Calendar No. 203

100TH CONGRESS
1st Session

SENATE

REPORT
100-85

UNITED STATES TRADE ENHANCEMENT ACT OF 1987

REPORT

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

TO ACCOMPANY

S. 1409

together with

ADDITIONAL VIEWS

JUNE 23, 1987.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE

91-010 WASHINGTON : 1987

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UNITED STATES TRADE ENHANCEMENT ACT OF 1987

JUNE 23, 1987.—Ordered to be printed

Mr. PROXMIRE, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany S. 1409]

INTRODUCTION

On May 19, 1987, the Senate Banking Committee marked up and ordered to be reported a bill, the United States Trade Enhancement Act of 1987, to amend the Export Administration Act of 1979, to amend the Export Trading Company Act of 1982, to enhance the trade promotion activities of the United State Government, to provide for greater long-term exchange rate stability, to alleviate the international debt problem, to ensure fairer treatment of United States banks and financial institutions in foreign markets, and to amend the Foreign Corrupt Practices Act of 1977.

PURPOSE OF THE LEGISLATION

The United States Trade Enhancement Act of 1987 is a seven-title bill whose objective is strengthening the ability of United States industries and financial institutions to compete in international markets at a time when more than one-fifth of the U.S. economy is directly involved in international trade and more than seventy percent of all U.S. products must compete with foreign products. The cumulative trade deficits of over $500 billion, built-up by the U.S. since 1982, have made this country the world's largest debtor nation and underscore the need of our economy to compete internationally.

The U.S. foreign debt obligation must be addressed now, for it constitutes a claim against our nation's output, limiting our ability to create new productive capacity and to ensure a rising standard of living for our people. The key to addressing the debt problem and restoring balance lies in significant expansion of U.S. exports. This bill accordingly attempts to improve U.S. export capabilities by: streamlining export controls consistent with maintaining our national security; facilitating the development of export trading companies; clarifying ambiguities in our country's anti-bribery statute; setting forth a framework for cooperation between the Congress and executive branch to develop long-term reforms that can provide greater exchange rate stability; improving the U.S. Government's trade promotion activities; giving the government new authority to improve the access of U.S. financial institutions to foreign markets; and setting forth a framework to assist in resolving the international debt problem that limits markets for U.S. exporters and raises concerns about the safety and soundness of U.S. banks.

History of the Legislation

The issues addressed in the various titles of the Unites States Trade Enhancement Act of 1987 are not new and the Banking Committee has held extensive hearings and reported legislation on most of them in recent years. For example, in 1986 the Committee reported out S.2815, the Export Revitalization Act which addressed the nation's exchange rate and international debt problems, strengthened the government's export promotion programs and amended the Export Trading Company Act. The full Senate, however, failed to take up omnibus trade legislation in 1986 and the Committee's bill was not taken up on the floor. In 1981, 1983, and 1986 the Committee reported our amendments to the Foreign Corrupt Practices Act, although none were enacted into law.

During March and April of this year the Banking Committee's Subcommittee on International Finance and Monetary Policy conducted seven hearings on trade issues within the Committee's jurisdiction. Shortly after those hearings were completed, Senators Proxmire and Sarbanes, the Chairmen of the full Committee and the International Finance Subcommittee respectively, presented Committee members with Committee Print No. 1 dated May 1, 1987. During the Committee's May 19 markup sixteen amendments were presented to the print, of which the Committee accepted nine. At the conclusion of the markup, the Committee reported out the United States Trade Enhancement Act of 1987 on a voice vote.

More extensive histories of each of the seven titles of the Committee's bill, along with explanations of each of the titles and a section-by-section analysis of the bill follow below.

Overview

Title I of the bill addresses the issue of export controls and strikes a balance between the need for U.S. exporters to be able to compete effectively in international markets and the genuine security requirements of the United States in controlling the sale to the Eastern Bloc of high technology goods with military applications. Thus the bill would decontrol the sale of goods to countries which participate in the Coordinating Committee on Multilateral Export Controls (CoCom), and countries with bilateral export control agreements with the United States. Such decontrol would only apply to goods which fall below the technology level of the so-called PRC green line, while retaining in the Secretary of Commerce authority to require a license to such end-users of an export as the Secretary may deem appropriate or to countries which do not comply with the CoCom agreement.

Similarly, the bill would also decontrol the reexport to CoCom countries of U.S. goods, and of foreign goods containing U.S. components worth less than 20 percent of the value of the good into which they are incorporated to any destinations. It would, however, give the Commerce Secretary authority to license the reexport of finished goods or components he deems to be highly critical. The bill would also decontrol goods containing controlled parts or components worth less than 20 percent of the value of the good, unless the Commerce Secretary determines that the good as a whole would make a significant contribution to the military potential of a controlled country. In addition, the bill would provide for the decontrol of goods to other than controlled countries if a foreign availability determination were made, but the President could delay decontrol for eighteen months while he attempts to negotiate an end to the foreign availability, and Congress would have to be notified of the commencement of such negotiations.

In order to avoid delay in the implementation of the Export Administration Act, title I would set a firm 120-day time limit on foreign availability determinations by the Commerce Department so that if no determination is made within 120 days, the Secretary may not require a license for the export of the good in question. A firm time limit is also placed on the Defense Department's review of national security export license applications. If no recommendation is made within 20 days, the Commerce Secretary would have authority to approve or deny a license.

To improve enforcement of export controls, the bill would give the Commerce Secretary greater authority to issue temporary denial orders for exports if it would facilitate enforcement of the Act. It would also give the Secretary authority to deny an export license not only to an individual who has prior convictions for certain specified crimes, but also to corporations or business organizations under the control of the convicted person. The President would also be directed to enter into negotiations with the member governments of CoCom to: (1) improve cooperation with CoCom; (2) obtain agreements with non-CoCom governments; and (3) to restrict the export of goods and technology on the International Control List (ICL).

Finally, to guard against possible administrative abuse, parties would be given the right of judicial review under the Export Administration Act when a civil penalty or other sanction would be imposed for violation of the Act or when a temporary denial order is granted under the Act.

Title II of the bill is designed to give greater flexibility to bank-affiliated export trading companies to facilitate the export of U.S. goods and services while safeguarding the safety and soundness of the banks which are affiliated with the ETCs and maintaining the focus of the ETCs on the export of U.S. goods and services. ETCs would be allowed to count fees derived from facilitating exports between third countries as revenue derived from exporting so long as the fees are remitted to the U.S. and the aggregate amount of the fees in any one year did not exceed one-fifth of the amount of the revenues derived from promoting U.S. exports. In addition, the permissible assets-to-equity ratio of an ETC would be established at 15–1, and the $2 million inventory limitation would be removed and replaced by case-by-case review by the Federal Reserve. Also, the Commerce Department would be directed to establish a program to encourage and assist the development of other export intermediaries including export management companies which are not bank sponsored.

Title III of the bill strenghtens the export promotion activities of the Commerce Department. Regular review of the number of Foreign Commercial Service officers in U.S. diplomatic missions would be required, and the Commerce Secretary would be authorized to designate eight U.S. missions abroad at which the senior U.S. and Foreign Commercial Service officer would be able to use the diplomatic title of Minister-Counselor. The Commerce Secretary would also be directed to gather information collected by federal agencies on a country-by-country basis which would be useful to firms engaged in exports and to set up an information system to disseminate the data to private sector businesses and state export agencies.

Title IV of the bill addresses the issue of international economic policy coordination and exchange rates. The purpose of the title is to encourage the President to negotiate with other countries to achieve better coordination of macroeconomic policies, an improved balance of trade, and greater coordination of the participation of central banks in international currency markets where necessary to reduce severe fluctuations in currency values. The title also directs the President to initiate negotiations with countries which manipulate the rate of exchange between their currency and the dollar for the purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade. The purpose of the negotiations would be to ensure that such countries regularly and promptly adjust the rate of exchange between their currencies and the dollar.

In addition, the Secretary of the Treasury would be required to submit an annual written report to the Congress and to testify annually before the Congress on the conduct of international economic policy, much as the Chairman of the Federal Reserve Board is required to report and testify annually to Congress on the conduct of monetary policy. The Secretary would be required to report on the conduct of international negotiations, assess the ability of the U.S. to maintain a sustainable balance in its current account, state proposed changes in U.S. economic policy likely to impact our current account position, and analyze the exchange rate trends and economic policies of any countries with which the U.S. has substantial bilateral trade or capital flows.

Title V of the bill addresses the issue of international debt. The title finds that the international debt problem threatens the safety and soundness of the world financial system, the stability of the world trading system, and the political and economic stability of the debtor countries. Increasing growth in the developing world should be a major goal of U.S. international economic policy, and a broadened range of financing options should be considered in dealing with the debt problem.

The title would direct the Treasury to initiate discussions with industrialized and developing countries to propose the establishment of a multilateral financial authority which would be authorized to purchase sovereign debt of less-developed countries from private creditors at an appropriate discount, enter into negotiations with the debtor countries to restructure the debt, and assist creditor banks in the voluntary disposition of their loans. It is anticipated that support for the authority would come from the major industrialized countries, particularly from countries running strong current account surpluses. It is anticipated that the authority would have a close working relationship with the World Bank and the IMF; and would be a self-supporting entity, requiring no routine appropriation from any member government; and that it should have a specified termination date.

The title also addresses the international debt issue from the standpoint of bank regulation. The title takes the view that commercial banks should establish sufficient reserves against the risks inherent in international lending and, within regulatory constraints, should have significant latitude to restructure the terms and conditions on their existing international loans so that additional new lending is not the only option available to U.S. commercial banks in responding to the financial needs of heavily indebted countries. The Federal banking agencies are directed to study any regulatory or accounting barriers to exchange of foreign debt-for-equity, and the Treasury Secretary is directed to instruct the U.S. Executive Director of the World Bank to initiate discussions with other directors of the Bank on the appropriate role for the Bank and the International Monetary Fund in supporting debt-to-equity swaps. The Federal banking agencies are also instructed to review other possible regulatory steps to encourage a reduction in the indebtedness of heavily indebted international borrowers in a way that would improve the overall asset quality of the banks.

Title VI of the bill seeks to encourage foreign countries to end discrimination against U.S. banking organizations and securities companies. It would amend the International Banking Act of 1978 by authorizing Federal banking agencies, with the prior approval of the President, to deny any application by a foreign banking organization from a country that discriminates against U.S. banking organizations. The title would also prohibit the Federal Reserve System from designating any person of a foreign country as a primary dealer in U.S. Government securities if that foreign country discriminates against U.S. companies in the underwriting or distribution of its government securities.

Title VII of the bill makes amendments to the Foreign Corrupt Practices Act of 1977, which was enacted to prevent U.S. corporations from using bribery of foreign officials as a means of obtaining or retaining business abroad. The Committee's amendments clarify certain ambiguities in the present statute which have caused concerns among U.S. businessmen without changing the basic intent or effectiveness of the law. It alleviates concerns that criminal penalties might be brought for inadvertent errors in complying with the law's books-and-records or accounting-control provisions. It also provides that businessmen can use a cost/benefit analysis in determining the level of detail required in their books-and-records and accounting systems. It provides that a company is not liable for violations of the books-and-records and accounting provisions by a subsidiary, which it does not control, if the company makes good faith efforts to cause the subsidiary to comply. The title consolidates in the Justice Department all jurisdiction with respect to civil and criminal enforcement of the anti-bribery provisions of the FCPA. It also changes the standard by which a corporation is responsible for illegal payments by its agents from a "reason to know" standard to a "direct or authorize expressly or by a course of conduct" standard. This will not change the Justice Department's present enforcement policy. Finally, the title provides certain exceptions and defenses to the law's anti-bribery prohibition for facilitating payments, none of which are intended to encompass corrupt payments either for the obtaining or retaining of business.

TITLE I.—AMENDMENTS TO THE EXPORT ADMINISTRATION ACT (EAA)

HISTORY OF TITLE I

In June 1985, the Congress completed over two years of work in dealing with export control issues by passing the Export Administration Act Amendments of 1985 (Public Law 99–64). This statute provides broad authority for the executive branch to control exports for purposes of national security, foreign policy and domestic short supply. The 1985 law extended the President's authority to control exports under that Act unil September 30, 1989. Concerns about how that law is being administered, raised in part by a report of a distinguished panel of the National Academy of Sciences, which will be discussed below, led the Committee to craft new amendments to the EAA for inclusion in omnibus trade legislation to be considered by the Senate.

The Subcommittee on International Finance and Monetary Policy of the Committee on Banking, Housing and Urban Affairs held oversight hearings on March 12 and 17, 1987 on issues related to the Export Administration Act of 1979 as administered by the Department of Commerce. National security controls, the Administration's views on foreign policy controls and the Administration's bill to amend the EAA were the subjects of the March 12 hearing. The March 17 hearing focused on export controls and the need for a better balance between assuring U.S. national security interests and international competitiveness in trade. Witnesses testifying at these hearings are listed below:

March 12, 1987

Malcolm Baldrige, Secretary of Commerce; Lew Allen, Jr., director, Jet Propulsion Laboratory and chairman of the National Academy of Sciences Panel on National Security Export Controls; Richard Cooper, professor, Harvard University and a member of the National Academy of Sciences Panel on National Security Export Controls; John McLucas, chief executive officer, QuestTech Corporation and a member of the National Academy of Sciences Panel on National Security Export Controls; Edward Derwinski, Acting Undersecretary of State; and Richard Perle, Assistant Secretary of Defense for International Security Policy.

March 17, 1987

John E. Pomeroy, a member of the American Electronics Association and president, Universal Instruments Corporation; Calman J. Cohen, vice president, Emergency Committee for American Trade; Charles Hough, Scientific Apparatus Makers Association and director, Export Administration, Honeywell Corporation; Allan I. Mendelowitz, senior associate director, Government Accounting Office; and Lawrence Brady, Sanders Associates and former Assistant Secretary of Commerce for Export Administration.

On May 1, 1987 a Committee Print, which contained 13 sections of law amending the EAA, was released to members of the Banking Committee. At the May 19, 1987 markup, the Committee adopted two amendments to title I of the Committee Print, one of which was an omnibus amendment. The title as reported contains 28 sections of amendments to the Export Administration Act. Twenty-six of these are amendments to the national security control sections of the EAA. Section 119 amends the Act's foreign policy controls and section 120 amends the FAA's short supply controls on exports of refined petroleum products.

BACKGROUND

For most of its history, the United States did not have controls on exports. This changed in 1940 when Congress passed the Export Control Act to permit the U.S. to conduct full scale economic warfare against the Axis powers by cutting off all U.S. exports to those countries and by blacklisting companies in neutral countries doing business with the enemy. These controls expired after the war, except insofar as they were maintained to prevent the export of items in short supply in this country such as steel. In 1947, as U.S. relations with the Soviet Union deteriorated, President Truman used his authority under the 1940 Export Control Act to place restrictions on American exports to the Soviet Union, and subsequently delegated Presidential power over exports to the Commerce Department.

Since the implementation of effective export controls depended on cooperation from our allies, the Coordinating Committee of Multilateral Export Controls, or CoCom, was created in 1949 to coordinate allied export control policies. CoCom membership consists of the NATO countries (except for Iceland) and Japan. Congress, in 1949, also completely rewrote the Export Control Act and began the practice of granting export control authority to the President for specified periods of time. That Act was renewed in 1951, 1953, 1956, 1958, 1962, and 1965. In 1969, Congress made major amendments to the Export Control Act and renamed it the Export Administration Act. That Act has also been renewed and revised several times in the last eighteen years.

NATIONAL SECURITY EXPORT CONTROLS

Preserving our National Security requires reasonable and appropriate export controls to prevent the Eastern bloc from acquiring military critical western technology. The evidence is overwhelming that the Soviet Union and its satellites have used U.S. and Western technological developments to rapidly improve their military capabilities in microelectronics, lasers, radar, precision manufacturing, and other areas.

Their acquisition of such technologies is not accidental. The Soviets run a massive, well-managed technology acquisition program which enables them to save significant amounts of time and money in their military R & D programs. It allows them to narrow the gap between our weapons systems and their own and to develop countermeasures to our own technological innovations. This necessarily forces the U.S. and its Western allies to spend more on defense programs. In the early 1980's, the U.S. tightened its export controls to help stem such acquisitions.

The U.S. business community has recognized this problem and has not been opposed to controls on items whose acquisition by the Soviets would be detrimental to our national welfare. U.S. exporters have been concerned, however, by export controls that are too broad, or which forbid them from making sales which are then made by companies from Japan or Europe. The 1985 amendments to the EAA attempted to strike the proper balance between these two concerns and delegated to the executive branch the authority to administer them in a reasonable manner.

RENEWAL OF THE EXPORT CONTROL DEBATE

The debate over U.S. export control policy was renewed this year in the context of concern about overall U.S. trade policy and competitiveness. A report issued by the National Academy of Sciences entitled "Balancing the National Interest: U.S. National Security Export Control and Global Economic Competition" is the most recent comprehensive review of our national security control system and its effectiveness in denying the Soviets access to Western technology. This report, which was produced by a special panel under the chairmanship of General Lew Allen, former Chief of Staff of the U.S. Air Force and presently director of the Jet Propulsion Laboratory of the California Institute of Technology, was released in December 1986. The panel, which included former Secretary of Defense Melvin Laird and former CIA Deputy Director Bobby Inman, concluded that there is not only extensive targeting, but also damaging acquisition of Western technologies and end products by agents of the Soviet Union and its Warsaw Pact allies. On this basis, the NAS report stated unequivocally that there is a need for national security export controls.

The report also points out, however, that while there is significant diversion of Western technology, espionage alone accounts for a high proportion of successful Soviet acquisition activities. The report concludes that the current export control effort is spread too broadly across too many technologies and products, many of which are currently available abroad in sufficient quality and quantity as to be beyond the feasible reach of CoCom—much less U.S.—control schemes. Such overbroad controls harm our industry's economic vitality and thus our national security. They cause U.S. businesses to lose sales abroad to foreign competition undermining their economic vitality. The panel recommended that executive branch decisions concerning national security export controls accord greater importance to maintaining U.S. technological strength, economic vigor, and allied unity. The report of the NAS panel served ase a catalyst for various proposals to narrow the scope of U.S. export controls. The Administration itself proposed changes to the current law in order to reduce burdensome controls that do not contribute to our national security.

During the March 12 oversight hearing on the Export Administration Act, Secretary of Commerce Baldrige, the first witness, said that the export control amendments in the President's Competitiveness Initiative were needed "to bring about the balance we have all been seeking to protect national security without impeding legitimate trade." General Lew Allen, the chairman of the NAS panel mentioned above, stated that the problem with America's export control program lay not with the Export Administration Act Amendments of 1985, but rather with the way that law was being administered. General Allen told the Committee that the Administration's export policy process was in "disarray", with the Commerce, Defense, and State Departments unable to settle their differences. He noted that mechanisms such as the National Security Council, which were supposed to resolve interagency conflicts, failed to provide leadership and that the Defense Department exercises a *de facto* veto over proposals of the Commerce Department. A witness for the American Electronics Association told the Committee that "Congress wrote a good law when it acted in 1985 amendments to the Export Administration Act. Ample authority was provided for the executive branch to make changes in the export control process for the benefit of national security as well as exporters." General Allen agreed, pointing out that most changes to export controls recommended by the NAS "could be accomplished by administrative action." The NAS report found that "although appropriate statutory authority appears to exist, the U.S. policy process for national security export controls lacks proper direction and affirmative leadership at the highest levels of government."

Concerned that an overly burdensome licensing system was hurting the technological strength of important U.S. industries with no benefit to our national security, the Banking Committee decided that further legislation was needed to streamline U.S. national security export controls. The Committee acted in order to enhance the competitive position of U.S. companies in international markets, while focusing control efforts on truly critical technologies.

The Committee's amendments to the Export Administration Act can be discussed under five headings.

1. Reduction of the Number of Controlled Items

The Commerce Department has the principal responsibility for determining which goods need export licenses before they can be exported. Such items are placed on the Commodity Control List (CCL). Critics of the export control system argue that too many low technology items are on that list. General Allen of the NAS panel testified, for example, that "it is necessary to reduce the number of items that the U.S. restricts in order to get focus and agreement on the most critical items that need protection." A witness from the General Accounting Office (GAO) testified that "the list of controlled items is too large. Almost half of the export license applications received each year could be eliminated without affecting national security." Other witnesses contended that there is a "foreign availability" requirement under the EAA to remove items from the CCL that are available to the Soviet bloc, but that provision is not properly utilized by the Administration. Mr. Charles Hough of the Scientific Apparatus Makers Association (SAMA) testified that "foreign availability determinations are delayed in part because the government agencies do not respond in a timely manner to Commerce's request for input into such determinations." The Committee reported several provisions designed to reduce the number of goods needing export licenses. Among other things these provisions aim to remove national security controls from low technology items and items which the Soviet can obtain from other countries.

(a) Exports to Members of CoCom.—Section 104 of title I eliminates the license requirement for exports to CoCom countries and countries which have bilateral export control agreements with the U.S. under section 5(k) of the Export Administration Act if the exports fall below the technology level of goods which CoCom governments allow to be shipped to the People's Republic of China (PRC) with only a notice requirement to the other member governments of CoCom. This level of technology is known as the PRC greenline. In order to prevent our export control policy to CoCom countries from being tied to our relations with the PRC, the bill "delinks" the PRC from exports to CoCom by providing that the greenline level as of May 6, 1987, is the level for delicensing exports to CoCom and Section 5(k) countries. This leaves the Commerce Department free to adjust the levels of exports to the PRC as our political relations with that country dictate and to adjust the CoCom level separately after that date. Section 114 requires the Secretary of Commerce to make annual reviews and adjustments of the PRC greenline and CoCom decontrol levels. In 1986, the Commerce Department issued 116,053 export licenses. Almost 40,000 of these licenses were issued for exports to CoCom countries. The Commerce Department estimate that this section will reduce by 20,000 the number of licenses issued to U.S. companies for exports to CoCom countries.

(b) Exports to Noncontrolled Countries.—Section 105 of this title delicenses exports to noncontrolled countries which fall below the so-called AEN (Administration Exception Notice) technology level set by CoCom. The AEN level is a lower level of controlled technol-

ogy. Presently CoCom requires only that a notice of sale of an export of this level of technology to a controlled country be provided to CoCom's participating governments. The Commerce Department estimate this provision should reduce by 24,000, or by about 20 percent the total number of export licenses issued in 1986.

(c) Foreign Availability Determinations.—Sections 112, 113, 117, and 118 of title I all deal with foreign availability, i.e., the condition under which the U.S. should not control items that are already available to the Soviet Union and its allies. Control over commodities freely available to the Soviets from non-U.S. sources unnecessarily limits the ability of U.S. firms to compete abroad. Congress first included foreign availability provisions in the FAA in 1979. In 1985, the Congress expended considerable effort refining the foreign availability provisions of the Export Administration Act to expedite the removal of ineffective controls and improve the ability of U.S. business to compete abroad on a more equal footing. Section 4(c) of the Act clearly states:

> . . . the President shall not impose export controls for foreign policy or national security purposes on the export from the United States of goods or technology which he determines are available without restriction from sources outside the United States in sufficient quantities and comparable in quality to those produced in the United States so as to render the controls ineffective in achieving their purpose, unless the President determined that adequate evidence has been presented to him demonstrating that the absence of such controls would prove detrimental to the foreign policy or national security of the United States.

In addition, sections 5(b) and 6(b) detail specific foreign availability consideration applicable, respectively, to national security and foreign policy controls. Despite this Congressional attention, the Commerce Department's implementing regulations, and the establishment of a separate organization within the Commerce Department to make foreign availability determinations, very few affirmative findings have been produced.

The principal obstacle to responsible and expeditious review of foreign availability seems to be less the analytical review process itself than disagreements among the various U.S. Government agencies. The Commerce Department has generally wished to proceed with decontrol, while the Defense Department has vigorously contested foreign availability, i.e., whether a specific good is available in sufficient quality and quantity so as to moot the purpose of the controls. Since carefully considered judgments may emerge from such a process, there is nothing inherently wrong with such disagreements if they can be resolved in a timely manner. However, experience with the procedure over a period of time demonstrates that the Administration has been unable to resolve the debates and the Congressional intent behind such provisions has been frustrated.

To cure this problem, the Committee bill makes both procedural and substantive changes in the foreign availability provisions of the Act. Section 118 of the bill clarifies that the Officer of Foreign

Availability in Commerce shall, at the request of the Secretary and consistent with protection of intelligence sources and methods, be provided access to all relevant information on foreign availability. This provision will ensure that the Secretary's decisions will be based on information from all sources and that no necessary information will be denied to the Secretary. Section 112 places time limits and a notice requirement on the Secretary of Commerce so that the public knows when a foreign availability assessment is being made and has an opportunity to comment and know that a final judgment must be made within a time certain (120 days maximum).

With respect to substantive issues, it should be noted that under the current law foreign availability determinations focus on the question of availability in controlled countries, that is the East Bloc. In this regard, once foreign availability is established in the Bloc, national security controls on exports of products are removed for all destinations. The current foreign availability provisions, however, do nothing to alleviate the burdens of unilateral U.S. export controls on products that are available in the free world. Since the vast bulk of business by U.S. exporters is concentrated in free world countries, the foreign availability provisions in the current law did not help most exporters.

The Committee therefore, decided in section 117 of its bill to add a provision to the EAA dealing with foreign availability to other than controlled countries. This provision governs items available in a non-controlled country, other than under an export license from a member of CoCom or a Section 5(k) country. Under the provisions, the Secretary may not, after the determination of "foreign availability" is made, require a validated license for the export of such goods or technology to any country to which the country, where foreign availability has been established, does not control export of the good or technology. The President can still require controls if he determines that the absence of export controls would prove detrimental to the national security of the United States. In the later case, the President would have a maximum period of eighteen months to negotiate away the foreign availability and if he failed to do so, the item would be delicensed. A similar opportunity to negotiate away foreign availability governs for findings of availability to controlled countries. The reasoning underlying section 117 is that if a free world country has available in abundance any item that is controlled by the U.S., there is no point in regulating export sales of such items to that country by our companies. The presumption is that export controls on the items do not make sense since the Soviets could obtain the items in that other country if they wished.

(d) Unilateral Controls.—The United States maintains a number of unilateral national security export controls—controls which it has been unable to convince its CoCom partners to adopt because they do not share U.S. concerns about the critical nature of the items and are not interested in instituting multilateral controls on them. The Committee determined that unilateral controls maintained in the face of foreign sources of supply are pointless and should be eliminated unless the U.S. has underway an active effort to negotiate multilateral controls. Section 109 of this title states

that the Secretary of Commerce "should eliminate each year all items on the control list maintained unilaterally by the United States except for controls of goods or technology for which foreign availability does not exist or with regard to which the United States is actively pursuing negotiations to achieve multilateral cooperation."

(e) Sunset Provisions.—Section 110 is also aimed at shrinking the control list. This provision requires that if an item on the control list is below the PRC greenline level of technology, its inclusion of the list should be reviewed at least once every two years. If such a review has not been conducted and a person requests a review by the Secretary, the item must be decontrolled unless the Secretary determines within 90 days that controls are still needed. If no review is made within the extra 90 day period this provision requires that the item must be decontrolled.

(f) Goods Containing Controlled Parts and Components.—The U.S. traditionally imposed national security export controls on a good only if the entire good itself would make a significant contribution to the military potential of any country or combination of countries which would prove detrimental to the national security of the United States. Individual component parts were not a factor in determining whether or not to impose controls. In the 1980's, computers and electronic items tended to be treated differently and these goods were controlled if they contained microprocessors. In 1985, the Congress added section 5(m) to the EAA to decontrol goods containing embedded microprocessors when the overall functional characteristics of the goods did not merit control. While that provision was initially helpful to U.S. instrument exporters, technological advances have occurred since its enactment. Instead of using embedded microprocessors to operate their goods, U.S. corporations are now buying commercial microprocessors and personal computers and incorporating these in their products. In section 116, the Committee expands section 5(m) of the EAA to prohibit controls on goods that contain controlled parts and components, in addition to just embedded microprocessors, if the parts or components are essential to the operation of the good, are customarily included in the good, comprise less than 20 percent of the value of the good, and the overall good in not controlled. This provision precludes separate licensing requirements for subsystems and focuses the licensing and control requirement on the overall system. The practical effect of this provision is that to the extent the Soviets seek to obtain a controlled subcomponent by buying an overall system, they would have to pay at least five times the market price of that subcomponent.

2. Reexport Controls

The United States, alone among CoCom countries, requires approval in addition to whatever licensing the local foreign government may require, for reexport of sensitive U.S. origin products from the country to which they were originally licensed. The reexport issue arises in two contexts: (1) the resale by a company in one country of a previously licensed U.S. good to a new end-user in another country, or (2) the incorporation of previously licensed U.S. goods and components into a foreign made product. Secretary of

Commerce Baldrige testified on March 12 that "One multibillion dollar European electronics company has noted that it is deliberately avoiding American component parts for its products to avoid U.S. reexport controls on such products." Calman Cohen, vice president of the Emergency Committee for American Trade (ECAT), told the Committee at its March 17 hearing that "Foreign customers of U.S. products are tiring of U.S. reexport licensing requirements and are switching their purchases to non-U.S. suppliers in order to avoid the uncertainties of being subject to U.S. export control authorities." While sympathetic to such concerns, the Committee was also concerned that the Soviets might acquire U.S. strategic goods simply by repurchasing them once they are shipped abroad.

To resolve this dilemma, the Committee adopted section 106 of the Committee bill. Part (a) of this provision eliminates the license requirement for reexports of finished U.S. goods to CoCom countries or countries which have bilateral export control agreements with the U.S., the so-called Section 5(k) countries. The Secretary of Commerce is permitted to require the maintenance of reexport controls on goods "which after consultation with the appropriate technical advisory committees, he determines to be unilaterally controllable by the United States." While the Committee's bill does not amend those sections of the Act relating to technical advisory committees (TACs), the Committee believes the Department of Commerce has not made full use of these sources of technical expertise in the way Congress intended.

The purpose of TACs is to create a two-way policy dialogue between technical experts in industry who are familiar with products subject to controls and Commerce Department policymakers. Some TACs currently operate at less than full strength because industry representatives don't believe their input will make any difference in the policy process. The Committee urges the Secretary to strengthen the voice and visibility of TACs and establish a better two-way dialogue with them.

Part (a) of this provision also requires written notice to be given to the Secretary at the time of reexport. This will ensure that a "paper trail" is maintained on reexports with CoCom so as to protect the ability of U.S. enforcement officials to trace goods and prevent diversions or prosecute diverters.

Part (b) of this section provides that no reexport controls may be required on a foreign produced product if the U.S. component part is 20 percent less of the dollar value of the final product. This provision also gives the Secretary residual authority by requiring "a license for the reexport of incorporated goods or technology to any country if the Secretary determines such goods or technology is highly critical." It should be noted that items below the AEN level will not require reexport authorization unless they are reexported to proscribed countries.

3. Interagency Disputes

Under the Export Administration Act of 1979, as amended, the Secretary of Commerce administers the export control system and issues export licenses. However, section 10(g) of the Act includes special procedures for the Secretary of Defense to review some kinds of export license applications. That section of the law states that the Secretary of Defense is:

> authorized to review any proposed export of any goods or technology to any country to which exports are controlled for national security purposes and, whenever the Secretary of Defense determines that the export of such goods or technology will make a significant contribution, which would prove detrimental to the national security of the United States, to the military potential of any such country, to recommend to the President that such export be disapproved.

The Act, however, did not specifically define countries "to which exports are controlled for national security purposes," and this omission led to interpretative differences between Commerce and Defense Departments. In mid-1981, the Defense Department asserted that it had responsibility under the Act to review export license applications to free world destinations, including responsibility to (1) generally monitor the potential for diversion from such countries and (2) specifically evaluate the diversion potential of an end-user and assess the validity of an applicant's end-use statement.

The Commerce Department, on the other hand, interpreted Defense's responsibility differently. At that time, Commerce asserted that Defense had the authority to review license applications to Soviet bloc destinations only, and therefore it was not appropriate for Defense to assess the diversion potential of end users in free world countries as part of the licensing process.

In 1983, the House of Representatives advocated limiting the role of the Secretary of Defense to reviewing exports to controlled contries. The Senate, on the other hand, passed legislation clarifying the EAA by stating specifically that the Secretary of Defense could review license applications to certain free world countries if there was a risk of diversion of exports from such countries to proscribed destinations.

In January 1985, President Reagan issued a directive to resolve the interagency conflict. Prior to that directive, a September 1981 interagency understanding gave the Defense Department the right to review only licenses for the very highest technology computer-related exports to non-controlled destinations. Whether or not Commerce referred such applications to Defense depended on specific operational characteristics of the item proposed for export and on whether the end user was in a special category, such as a government agency. The 1985 Presidential directive expanded the scope of the 1981 understanding. Added to Defense's review of proposed exports to the Soviet bloc and China were all licenses for 8 product categories exported to 15 free world destination.[1] In a September 1986 report to Congress on this Presidential directive, the GAO

[1] The General Accounting Office in a September 1986 report to the Congress indicated that the 15 noncontrolled countries to which DOD could review exports under the directive were Austria, Finland, Hong Kong, India, Iran, Iraq, Lichtenstein, Libya, Malaysia, South Africa, Singapore, Spain, Sweden, Syria, and Switzerland. The product groups included computers; software; electronics and semiconductor manufacturing; measuring, and calibrating equipment; micro and integrated circuits; and carbon technology and manfacturing equipment.

stated that at the time of its reveiew no CoCom destinations were subject to Defense review.

Despite the Presidential directive interagency disputes have continued to plague administration of the Export Administration Act and have prevented timely decisions on some export licenses. This problem is not inherent in DOD's role in reviewing critical exports and there was no proposal by Committee members to restrict DOD's license review role to only exports to controlled countries. Rather, it appears that criticisms of DOD's role stem from the Administration's failure to adopt measures to resolve interagency disputes in a timely manner. The Committee, therefore, enacted procedures to resolve such disputes. Section 121 of title I amends section 10(g) of the Export Administration Act (EAA) to provide that the Secretary of Defense has 20 days to make a recommendation on any license referred to him for review. If the Secretary makes no recommendation within 20 days the Secretary of Commerce would have complete authority to approve or deny licenses. The section further, provides that during his 20 day review the Secretary of Defense could recommend that the license be approved, approved subject to conditions, or denied. In the last case, the Secretary would make his recommendation to the President. Present law provides that "If the President notifies the Secretary (of Commerce) within 20 days after receiving a recommendation from the Secretary of Defense that he disapproves such export, no license or other authority may be issued for the export of such goods or technology to such country". The Committee understands this provision to mean that the President has 20 days to make a decision on export license disputes referred to him and fully expects that the President will make final decisions on all export licenses referred to him within that period so exporters will have timely decisions on whether they can export items. The Committee further amended section 10(g) of the present law by deleting subsection (4). That provision presently requires the President to notify the Congress whenever he overrules a recommendation from the Secretary of Defense to deny an export license. The Committee found that provision was too intrusive on a Presidential prerogative, gave excessive influence to DOD, and had the effect of delaying timely decisions on the granting of export licenses.

The Committee also adopted a provision (section 107) applying the same dispute settling procedure and time frame with regard to determining whether items should be on the Commodity Control List (CCL). This provision is intended to provide a means to break interagency deadlocks so that the control list is pruned and contains only those items essential to the protection of our national security. Finally, in section 128, the Committee charged GAO to submit a report to it not later than March 1, 1989 with regard to how these and other procedural improvements to ensure the efficient administration of export controls are being implemented. The Committee wants such report by March 1, 1989 so it can be used in deliberations about what changes would need to be made in the EAA before it expires on September 30, 1989. The Committee intends to utilize such report prior to reauthorization of the EAA in 1989.

4. Improvement of CoCom

The Banking Committee has made certain modifications to the U.S. export control system on the basis of an increased reliance on the effectiveness of the export control programs of our allies within CoCom. Sections 108 and 115 of title I are designed to increase the effectiveness of U.S. participation within CoCom. Section 108 provides, among other things, that the Commerce Department shall be responsible for formulating the proposals presented by the United States at CoCom meetings. This provision is not intended to infringe the authority of the Department of State as the chief U.S. negotiator at CoCom meetings. Rather, it is designed to ensure that the agency with the technical expertise and responsibility for compiling the CCL will also play the principal role in formulating proposals to add or delete items from the multilateral control list. Section 115 emphasizes the need for strengthened enforcement of multilateral export controls. As the U.S. relies more on multilateral export controls to safeguard its national security, it is essential that every effort be made to strengthen the enforcement programs of our allies.

5. Improved Administration

(a) Under Secretary.—In 1985, the Congress added section 15(a) to the EAA establishing an Under Secretary of Commerce for Export Administration. The Banking Committee reported that provision of law in 1983 because it believed "export administration has a far-reaching effect on the national security, foreign policy, and economic strength of the country . . . and it is essential that the responsibility for export administration be raised at least to the Under Secretary level." In 1983, the Committee made clear its expectation that "sufficient resources . . . would be devoted to export administration under the new Under Secretary." Since that provision was enacted into law in June 1985, the Commerce Department has delayed creating the office for various reasons. In 1986, the Congress extended the deadline for establishing this office until October 1, 1987. Sections 126 and 127 of title I facilitate the establishment of this office by clarifying that the Under Secretary will have responsibility for short-supply controls and Defense Production Act and all national security programs. These sections also set aside certain funds in the Commerce Department's budget to cover the start-up and operating costs of the new office. The Committee wants to ensure that this important provision of law, particularly in view of the new responsibilities title I gives to the Commerce Department, will be implemented by the executive branch without further delay.

(b) Prior Convictions.—Section 11(h) of the EAA authorizes the Secretary of Commerce to bar persons convicted of violating specified laws, including the Arms Export Control Act, from being eligible, at the discretion of the Secretary, to apply for or use any export license for a period of up to 10 years from the date of conviction. Section 123 of title I makes technical changes to this Section by including the Export Administration Act among the laws referenced. It also provides that the Secretary's authority to deny

exports can apply to any person, firm, corporation, or business organization linked to the convicted person.

(c) Temporary Denial Orders.—Section 13(d) of the EAA gives the Secretary of Commerce the right to issue a temporary order denying a person a right to export if that is necessary to prevent an imminent violation of the Act. Section 125 of title I amends the EAA to provide that a temporary denial order can be obtained not only to prevent an "imminent" violation, but also where necessary "to facilitate enforcement of the Act." The "imminent" violation standard currently in the EAA has limited the Department's ability to obtain temporary denial orders in instances where such an order would serve legitimate preventive enforcement purposes, such as where an indictment has been handed down or where, for a variety of reasons, documentary evidence that a violation is "imminent" cannot be obtained.

(d) Judicial Review.—Congress in the past, because of the important national security and foreign policy authorities given to the executive branch under the EAA, decided to exempt decisions taken under the law from the judicial review provisions of the Administrative Procedures Act. Section 124 of the Act makes limited exceptions to this overall exemption policy. It gives parties a right of judicial review under the EAA when a civil penalty or other sanction would be imposed for a violation of the Act or when a temporary denial order is issued under this Act. Other provisions of the EAA remain exempt from even this limited judicial review provision. For example, the government's right to establish a control list and make licensing decisions are not subject to review.

(e) Trade with the People's Republic of China (PRC).—Section 4(a)(2)(A) of the EAA presently provides authority for the Secretary of Commerce to issue distribution licenses which permit an exporter to make multiple exports of a range of goods within a particular category of technology designated by the license. This is in contrast to an individual validated license which applies only to the export of the particular goods described in the license. In 1985, when Congress established the distribution license, it prohibited the Secretary from utilizing such licenses for exports to controlled countries. Section 101 of title I would make an exception to that general prohibition and permit the Secretary to issue distribution licenses for exports to the PRC. It does not require them.

Section 111 of title I provides special authority for the Secretary, at his discretion, to licenses items for trade shows in the PRC, even though the item would not be eligible for an export license to that country. This provision is prompted by a desire to allow our exporters to keep pace with those from other CoCom countries who are permitted to send their latest models and equipment to trade shows in China notwithstanding the fact that they are above the technology level permitted to be sold in China under CoCom agreements. The Committee noted that the level of technology that may be shipped to China has been rising rapidly in recent years. Thus what cannot be licensed to China today might well be permitted in the future and trade shows are a process of showing future wares.

The Committee intends that the Secretary of Commerce and the exporter receiving a license should take every caution to ensure that goods licensed under this special provision are safeguarded from improper use while in the PRC, and are promptly removed from that country once the trade show is over.

The Committee intends that these two amendments will assist in ongoing efforts to improve our country's economic links with the PRC.

(f) General License for Reliable End-Users.—Section 4(a)(3) of the EAA presently provides that the Secretary of Commerce can issue general licenses "authorizing exports, without application by the exporter." Section 102 of title I requires the Secretary to include in the list of items that can be shipped pursuant to a general license "exports to qualified foreign parties that the Secretary has certified have a high expectation of being reliable end-users." The Committee intends that the Secretary use this authority to permit unrestricted exports to government departments and agencies of CoCom and Section 5(k) countries. It should also be used for shipments to commercial and other enterprises in such countries "where the government can establish the general policies or control the day-to-day operations of the entity."

(g) Fees.—Section 103 of title I provides that the Administration may not charge any fees in connection with export license applications. In a period when exporting must be encouraged, the Committee wants to make sure that processing of export licenses is not looked at as a new source of revenue for the government.

(h) Sanctions for Export Violations.—Committee amendments to the EAA place increased reliance on the effectiveness of the multilateral export control efforts of our CoCom allies. In order to encourage companies in CoCom countries to cooperate with the export control efforts of CoCom, section 122 of title I provides that foreign companies violating national security export controls that have been agreed upon within CoCom "may be debarred from contracting with any department, agency, or instrumentality of the United States for not to exceed five years."

The Secretary of Commerce would have full discretion to ban any or all new contracts between any U.S. Government entity and the foreign person who has violated CoCom national security controls. The sanctions in this provision may be applied in the case of violations under investigation during Committee and Senate consideration of the legislation as well as violations that are discovered or committed after that time. Any non-United States person in this provision is intended to include both the person or corporation directly responsible for the violation and parent and subsidiary corporations of the violator. The provision applies to all non-U.S. persons, even to joint ventures with U.S. persons. The Committee believes violators of CoCom controls should be on notice that they may have to choose between illicit trade and contracting with the U.S. Government. It makes no sense to permit foreign companies to sell items illegally to the Soviets that may increase our defense costs, and then to benefit by contracting with the U.S. Government to gain profits from our increased defense spending.

Foreign Policy Controls

Section 6 of the EAA permits the President to control exports to carry out the foreign policy of the United States. Because the Committee is concerned that such controls may sometimes impose costs on U.S. exporters that are not commensurate with the foreign policy gains, section 119 of title I adds a new provision to section 6(a) of the EAA requiring the President to employ diplomatic alternatives to export controls to express the displeasure of the United States with specific actions of foreign nations when the proposed target of the controls can use available foreign goods to evade the impact of the proposed controls. This section also provides that replacement parts for a good that has been lawfully exported are exempt from foreign policy controls unless controls are specifically placed on these parts.

Short Supply Controls

Section 7 of the EAA permits the President to control the export of items in short supply in this country. Section 120 of title I provides that no controls should be placed on the export of refined petroleum products that are refined in the United States "unless the President determines that such controls or restrictions are necessary." This section is a reaffirmation of Presidential authority under present law.

Title II.—Export Trading Company Amendments

HISTORY OF TITLE II

On March 25, 1987, the Subcommittee on International Finance and Monetary Policy held a hearing to review the implementation of the Export Trading Company Act of 1982. The witnesses at the hearing were: Alexander H. Good, Director General, U.S. and Foreign Commercial Service; R. David Luft, Deputy Assistant Secretary for Services, Department of Commerce; Manuel H. Johnson, Jr., Vice Chairman, Federal Reserve Board; Kenneth W. Rosenberg, president, First Interstate Trading Company; and Kenneth Barovick, executive director, National Federation of Export Associations.

On May 1, 1987, a Committee Print was circulated to the members of the Committee on Banking, Housing, and Urban Affairs. Title II of the Committee Print contained proposed amendments to the Export Trading Company Act of 1982. On May 19, 1987, the Banking Committee marked up the Committee Print and adopted title II without amendments.

BACKGROUND

The Export Trading Company Act of 1982 was passed by Congress in response to concerns that small and medium-sized U.S. companies lacked the expertise and the access to financing necessary to export successfully. Congress concluded that export trading companies (ETCs) would be a useful mechanism to help surmount some of the obstacles to U.S. exports.

The Act attempted to facilitate the development of export trading companies in three ways. Title I of the Act established an office within the Department of Commerce to promote and encourage the formation of bank affiliated export trading companies or export trade associations desiring antitrust clearance. The office was directed to provide information and advice to interested persons and to provide a referral service to facilitate contact between producers of exportable goods and services and firms offering export trade services.

Title II of the Act, known as the Bank Export Services Act (BESA), made a significant departure from the long standing policy of separating banking and commerce in order to promote the development of bank-affiliated export trading companies. Title II amended the Bank Holding Company Act of 1956 to permit bank holding companies to assume equity positions in operate bank-affiliated export trading companies, with the limitation that a bank holding company could neither invest more than 5% of its consolidated capital and surplus in an ETC nor lend more than 10% of its consolidated capital and surplus to an ETC. This change was undertaken in the belief that bank holding companies with international offices, experience in trade financing, and familiarity with U.S. domestic producers could play an important role in expanding the use of export trading companies in the United States. The Act provides that a bank holding company may invest in an ETC only after review by the Federal Reserve Board. The Board is required to determine whether the proposed investment may result in unsafe or unsound banking practices, undue concentration of resources, decreased or unfair competition, conflicts of interest, or whether the investment would have a materially adverse effect on the safety and soundness of the bank holding company.

Title III of the Act gave the Secretary of Commerce, after consultation with the Attorney General, authority to grant certificates of review to export trading companies under which an advance determination is made as to whether a proposed export activity is exempt from federal antitrust laws. The purpose of the certificates was to remove any presumed lack of clarity in antitrust laws as applied to non-U.S. business activities of American firms that might inhibit small U.S. producers and manufacturers from cooperating in their exporting efforts through export trading companies.

In the five years since the passage of the Export Trading Company Act, a limited number of export trading companies have taken advantage of the procedures provided by the legislation. Seventy companies have received Department of Commerce certificates for antitrust protection, and 28 of 42 bank-affiliated export trading companies remain in operation with a total authorized investment of approximately $86 million. The great majority of export trading companies in the United States, approximately 2,400, are not bank-affiliated and have largely not been impacted by the Export Trading Company Act.

DEVELOPMENT OF EXPORT TRADING COMPANIES

The relatively slow development of bank-affiliated export trading companies during the first five years of operation of the Bank Export Services Act has led to concerns that the regulations promulgated by the Federal Reserve Board pursuant to the Act have been unduly restrictive and have limited the use of ETCs. The Subcommittee on International Finance and Monetary Policy heard testimony from the Commerce Department and a representative of a leading bank-affiliated ETC on the need for adjustments in the

50% revenue test, the 10-1 leveraging ratio, and the $2 million inventory limit imposed by the Federal Reserve Board on export trading companies. The Subcommittee also heard testimony from Manuel Johnson, Vice-Chairman of the Federal Reserve Board, who strongly argued that the Federal Reserve Board's regulations have (a) not undermined the development of bank-affiliated ETCs and (b) carry out the intent of Congress that bank-affiliated ETCs focus their activities on the export of U.S.-provided goods and services and that the safety and soundness of the banks affiliated with ETCs be preserved.

While supportive of the Federal Reserve Board's approach to the regulation of export trading companies, the Committee did adopt adjustments to the regulations in sections 201, 202, and 203 of the legislation to facilitate the development of bank-affiliated export trading companies. In section 204 of the legislation, the Committee directs the Commerce Department's Office of Export Trade to establish a program to encourage and assist the development of non-bank-affiliated export management companies, which the Committee believes have not received sufficient support since the passage of the Export Trading Company Act. These legislative changes are described below.

The Committee notes that the slow growth and development of bank-affiliated export trading companies over the past five years may have been significantly influenced by the adverse economic climate that made exporting difficult for all sectors of the U.S. economy, as well as the unfamiliarity of U.S. bank holding companies and manufacturers with ETCs as vehicles for export trade. The Export Trading Company Act of 1982 was signed during the fourth quarter of 1982, when the U.S. economy was in a deep recession and the volume of exports had fallen more than 20% from its peak in 1980. Since that time U.S. output and employment have expanded, while U.S. exports have rebounded only moderately an still remain below their 1980 peak. The rise of the dollar against foreign currencies, the relatively sluggish growth of foreign economies, and the drop in imports by countries experiencing problems meeting their external debt obligations all contributed to the weak U.S. export growth that may well have had an impact on the development and growth of bank-affiliated ETCs.

In addition, U.S. manufacturers have not traditionally made widespread use of export trading companies as a vehicle for exporting their goods. The Federal Reserve points to an estimate that the 2000 American-owned trading companies active in U.S. in 1982 were involved in only about 10% of all U.S. exports. The slow development of export trading companies since the passage of the Export Trading Company Act in 1982 may be largely attributable to unfamiliarity with the vehicle of the export trading company, combined with an adverse economic climate. The Committee believes that additional experience in utilizing export trading companies, combined with the changes made in the legislation, will provide a fair opportunity for export trading companies to demonstrate their usefulness in promoting the sale of U.S. exports.

50 PERCENT REVENUE TEST

The Bank Export Services Act defines an export trading company as a company "which is organized and operated principally for purposes of exporting goods or services produced in the United States." Pursuant to the language of the Act, the Federal Reserve Board promulgated a regulation requiring that 50% of a bank-affiliated export trading company's revenue must be derived from exporting or facilitating the export of goods and services produced in the United States by persons other than the export trading company and its subsidiaries.

The purpose of the regulations was to carry out the intent of Congress that export trading companies focus their activities on promoting the export of U.S.-made goods and services, rather than importing goods from abroad or promoting third country exports (for example, exports from France to West Germany). The Bank Export Services Act represented a dramatic departure from traditional banking legislation by permitting participation by banking organizations in commercial ventures. This narrow exception to the traditional separation of banking and commerce was made for what was seen as the strong national interest in promoting the sale of U.S. exports as a means to expand economic growth and create jobs. The Federal Reserve regulation seemed well calculated to carry out this Congressional intent.

Under the regulation, third country exports promoted by bank-affiliated export trading companies are counted as non-export income. This requirement is based on the Federal Reserve's view that the Congress intended for bank holding companies to be permitted to invest in export trading companies under the Bank Export Services Act for the explicit purpose of facilitating the export of U.S.-made goods and services. If a bank-affiliated export trading company were permitted to count all of its fees from third country sales as export income, or even to exclude the fees from being counted as either export or import income, then the ETC would be able to devote virtually its entire business to third country export promotion. This was not the purpose for which Congress created an exception to the separation of banking and commerce under the Bank Holding Company Act.

In addition, it is possible that promoting third country trade might actually damage U.S. trade. Third country transactions promoted by export trading companies may serve as substitutions for U.S. exports. A sale made by a European country to Japan might preempt a potential U.S. export to Japan. Permitting export trading companies to focus their activities on promoting third country trade would put ETCs into direct competition with other U.S. companies that produce goods and services in the U.S. for export abroad, precisely the companies intended to be the primary beneficiaries of the Export Trading Company Act. Permitting export trading companies to engage in general trading activities without regard to promoting U.S. exports would shift the emphasis of the original statute from export promotion to promotion of international trade per se. This was not the intent of Congress in passing the Act.

For these reasons the Committee is supportive of the 50% revenue test promulgated by the Federal Reserve, and specifically as it is applied to third country exports. The Committee is cognizant, however, of the start up difficulties experienced by bank-affiliated export trading companies over the past five years, and the usefulness third country exports may have for ETCs attempting to develop business contacts overseas which may lead to future U.S. exports. In section 201 of the legislation, therefore, the Committee provides that the 50% revenue test would not apply during the first two years of the operation of a bank-affiliated export trading company, and that in determining whether the 50% revenue test has been met, not less than four consecutive years of the operation of an ETC must be taken into account (excluding the first two years). In addition, the legislation would permit fees derived from third country exports to be counted as export income if the fees are remitted to the United States (and therefore serve to improve the U.S. balance of payments) and if the fees do not exceed one-fifth of the revenue actually derived from promoting U.S. exports. Since 50% of revenue is required to be derived from promoting U.S. exports, one-fifth of that amount could be as much as 10% of the total income of the ETC.

The Committee believes that these changes will provide bank-affiliated export trading companies with sufficient flexibility to develop a successful exporting business without undermining the intent of Congress that bank-affiliated export trading companies focus on facilitating the export of U.S. goods and services.

LEVERAGING RATIO

The Federal Reserve Board requires that a bank-affiliated export trading company with an assets to equity ratio of more than 10–1 must have its notice reviewed in Washington rather than at a regional Federal Reserve Bank. However, in reviewing notices by banking organizations to invest in ETC's the Federal Reserve considers the assets to equity ratio of each proposed ETC on a case-by-case basis, taking into account, among other factors, the riskiness of the ETC's proposed activities.

In carrying out its duty to preserve the safe and sound operation of bank holding companies, the Federal Reserve must be able to examine carefully the capital structure and proposed leveraging ratios of bank-affiliated ETCs. Capital adequacy is a critical determinant of the financial strength of an ETC and of its ability to withstand unexpected adverse developments so as not to affect the financial resources of the parent bank holding company or the safety and soundness of affiliated banks.

U.S. banks are now required to maintain a minimum capital-to-total assets ratio of 6% (slightly less than 17–1). There seems to be little justification for a statutory rule allowing a capital-to-assets ratio for bank-affiliated export trading companies greater that that permitted banks since the business of ETCs is likely to be outside the normal range of banking activities and therefore subject to greater risks. Many factors must be taken into account in determining the appropriate assets-to-equity ratio of an ETC such as the nature of its business, the size of its inventory, and the size of the bank holding company's investment in the ETC. A case by case analysis is best suited to take all these factors adequately into account.

Even though the Federal Reserve reviews assets-to-equity ratios of ETCs on a case-by-case basis and has approved a leveraging ratio as high as 17–1, the Committee is sensitive to the concern raised in testimony by the Commerce Department that the current law discourages leverage ratios greater than 10–1 by requiring any ETC with a higher assets-to-equity ratio to submit its notice for review in Washington rather than at a regional Federal Reserve Bank. As a a result, section 202 of the legislation would forbid the Federal Reserve from disapproving a proposed investment by an ETC solely on the basis of its assets to equity ratio unless the ratio were greater than 15–1. This would bring the assets to equity ratio of export trading companies more closely into line with the ratio required of U.S. banks.

INVENTORY

The Federal Reserve Board currently requires that a notice by a bank holding company to invest in an export trading company must be reviewed in Washington rather than at a regional Federal Reserve Bank if the ETC will hold inventory in amounts worth more than $2 million. In the view of the Federal Reserve, taking title to goods through the accumulation of an inventory by an ETC involves risk sufficient that the Federal Reserve Board in Washington should have an opportunity to review such proposals on a case-by-case basis. The Federal Reserve has in fact reviewed and did not object to several notices in which projected inventory was substantially greater than $2 million.

Kenneth W. Rosenberg, president, First Interstate Trading Company, pointed out in testimony before the International Finance Subcommittee that the requirement that applications which anticipate an ETC holding inventories in excess of $2 million be referred to Washington discourages applications which envisage higher inventories. It can be reasonably argued that judgment about inventories should be made on a case by case basis depending on the nature of the export an ETC is promoting. Large ticket items, such an machinery, might justify higher inventories, which small ticket items, such as consumer goods, might require a lower inventory level.

Section 203 of the bill would prohibit the Federal Reserve from imposing a dollar limit on an ETC's inventory unless the Federal Reserve finds that the limit is necessary to prevent materially adverse effects on a bank affiliate of the ETC. The Federal Reserve conducts inventory review on a case by case under its current procedures. This provision would simply codify the Federal Reserve's current practice and would provide the Board with sufficient authority to exercise its supervisory powers in this area when necessary. It would also remove whatever disincentive effect the $2 million review requirement might impose.

EXPORT MANAGEMENT COMPANIES

The Export Trading Company Act of 1982 directed the establishment in the Department of Commerce of an office "to promote the establishment of export trade associations and export trading companies." The purpose of the office, called the Office of Export Trade, was to promote two kinds of trading companies—bank-affiliated export trading companies and those trading companies that were set up pursuant to the 1982 antitrust certification procedure.

Testimony before the Subcommittee on International Finance and Monetary Policy by Richard Barovick, executive director of the National Federation of Export Trade Associations, pointed out that the 500 export management companies which his organization represents have received no assistance from the Office of Export Trade because they don't fall into the two categories identified in the Act. As Mr. Barovick pointed out, export management companies are the export department or representative of small manufacturers, and they focus almost exclusively on exporting. Some have been in existence for over sixty years, and collectively assist approximately five thousand manufacturers a year and promote approximately $2.5 billion worth of exports. In addition, there are perhaps two thousand other export promotion companies of various sorts in existence in the United States that don't fall into the categories provided for in the Export Trading Company Act.

Section 204 of the legislation directs the Office of Export Trade of the Commerce Department to establish a program to encourage and assist the operation of these other export intermediaries, including existing and newly formed export management companies. Section 205 directs the Secretary of Commerce to submit a report to Congress on the activities of the Department to encourage the formation and operation of export promotion intermediaries including export management companies, export trade associations, and export trading companies.

TITLE III.—EXPORT PROMOTION

HISTORY OF TITLE III

On March 25, 1987, the Subcommittee on International Finance and Monetary Policy held a hearing which reviewed the export promotion programs of the Commerce Department. The witnesses at the hearing were: Alexander H. Good, Director General, U.S. and Foreign Commercial Service, and R. David Luft, Deputy Assistant Secretary for Services, Department of Commerce.

On May 1, 1987 a Committee Print of the U.S. Trade Enhancement Act of 1987 was circulated to the members of the Banking Committee. Title III of the Committee Print made changes in the Commerce Department's export promotion programs. On May 19, 1987 the Banking Committee marked up the Committee Print and adopted title III with one amendment.

EXPLANATION OF THE PROVISIONS OF TITLE III

Responsibilities of Foreign Commercial Service Officers

Several measures are included in title III to strengthen and give direction to the mission of our Foreign Commercial Service officers. Section 301 of the bill directs the Secretaries of State and Commerce to review periodically the assignment of Foreign Commercial Service officers to United States foreign missions, to ensure that a sufficient number of such officers are assigned to the posts most critical to our commercial interests.

The Secretaries are also directed to extend the length of assignment of such personnel in order to ensure greater continuity and experience in a particular post. Personal contacts and local experience are crucial in an export sale, and it is important to provide adequate time for Foreign Commercial Service officer personnel to establish those contacts and to benefit from that local experience.

Each chief of a U.S. diplomatic mission to a country that is an important trading partner would be required to submit to the President and the Congress an annual report on the export promotion activities of that post. In the view of the Committee, this reporting requirement will help to ensure that these trade concerns, vital to our national welfare, will not be ignored.

Further, billions of dollars in support are made available each year to developing countries through the various multilateral development banks, such as the International Bank for Reconstruction and Development, the International Development Association, the International Finance Corporation, the Inter-American Development Bank, the Inter-American Investment Corporation, the Asian Development Bank, the African Development Bank, and the African Development Fund. It is the sense of the Committee that measures be taken to ensure that U.S. suppliers have a fair opportunity to compete for the business generated by this multilateral development bank support. Our Executive Directors to these institutions should therefore provide our businesses with timely and appropriate information on projects and should also take action to ensure that U.S. suppliers are receiving fair treatment in the awarding of contracts. A Foreign Commercial Service officer should be assigned to each U.S. Executive Director to assist in this effort.

Collection and Dissemination of Trade Information

The Committee believes that the United States must make a concerted effort to increase exports if we are to reduce our trade deficit and maintain a healthy economy in the future. Only ten percent of U.S. firms are currently exporting their products, and about 250 companies account for most U.S. exports. Clearly, many additional companies have goods with export potential.

Section 302 of the bill directs the Secretary of Commerce to develop and maintain an export promotion data system targeted at the data and information on those industrial sectors and foreign markets which are of the greatest interest to business firms in the private sector which are engaged in or would like to be engaged in export-related activities and to State trade promotion agencies. The system is intended to include data and information which are collected through the Department's International Trade Administration office, organize it in a format most useful to private sector business firms and State trade promotion agencies, provide for the confidentiality of proprietary business information, and, disseminate such data and information, consistent with other provisions of law and upon request for a reasonable fee, in a timely manner to private sector entities and State trade promotion agencies.

The design of the system is to be that which provides that most effective means of disseminating the data and information electronically through the Department, or Department-designated offices, or through other available data bases. The system shall provide accurate and timely reports. It shall almost monitor, organize, and disseminate, within available Departmental resources, selected information on U.S. exports of goods and services by State or origin, port of departure, and importing country and U.S. imports of goods and services by country of origin, port of entry and State of ultimate destination. In addition, the system shall provide information on specific business opportunities in foreign countries and specific industrial sectors within foreign countries with high U.S. export absorption potential including information on the size of the market, existing product distribution systems and product competition. Further, the system shall provide accurate and timely reports on significant applicable laws, regulations and product specifications and standards required in particular foreign markets. The system shall provide information and up-to-date listings of appropriate government officials, trade associations and other relevant contact points. The system shall also provide any other information which may be useful to the U.S. exporting community for a particular foreign market, including relevant information on general economic conditions, common business practices, significant tariff and trade barriers, and other significant laws and regulations regarding importing and licensing. Data which may be excluded is that which is collected in connection with an investigation or the disclosure of which is prohibited by law. The Secretary is directed to consult with representatives of the private sector and State trade promotion agencies and to develop a report which includes their comments on the implementation of this system.

In the view of the Committee, U.S. exporters need the data listed in this section to develop their business plans. Moreover, State trade promotion agencies need the data to assess their current activities to help firms in their States expand their exporting, particularly the small and medium size companies. States also need the data to help identify new opportunities for the many U.S. corporations that have not yet entered international markets.

While improvements have been made in U.S. trade data in recent years, the information available to businesses and State trade promotion agencies is still not up to the high standards required in this important area. Available data and information are too often old and inaccurate, and they do not provide the detail needed for the U.S. exporting community for export promotion or to analyze U.S. trade performance. The provisions of the bill are designed to help close the gap. The Committee intends that the data system be a regular part of the Department of Commerce's trade promotion activities and directs the Secretary to report to the

Congress within six months of enactment of this Act on the implementation of this system.

Multilateral Development Bank Liaison

Several multilateral development banks do not have their main offices in the United States. These are the Asian Development Bank (Manila), and the African Development Bank and the African Development Fund (Abidjan, the Ivory Coast). In order to ensure that United States suppliers have a fair opportunity to compete for participation in the projects of these banks, the Committee in section 303 of the bill directs the Department of Commerce to establish a liaison office with these banks. This office would provide U.S. exporters with information relating to new projects, such as bid specifications and deadlines dates.

Rank of Foreign Commercial Service Officers

In 1979 Congress determined that the United States commercial trade interests carried out in our foreign missions would be better served if they were the responsibility of the Department of Commerce rather than the Department of State. Thus, since that time, Foreign Commercial Service officers have been employees of and reported to the Department of Commerce. The Commerce Department, recognizing the need to engage in senior level discussions within the host country to promote U.S. goods and services, believes it is very important to provide certain senior Foreign Commercial Service officers with the diplomatic title of Minister-Counselor. This action would further U.S. trade interests by providing better access to high ranking foreign government officials and policy makers.

It is the Committee's belief that designating a senior Foreign Commercial Service officer with the title of Minister-Counselor in strategically important foreign missions would benefit U.S. trade promotion activities. Thus, section 304 of the bill would authorize the Secretary of Commerce to designate eight United States foreign missions at which the senior Foreign Commercial Service officers will be able to use the diplomatic title of Minister-Counselor.

This provision would not result in any increased budgetary impact and it would provide senior Foreign Commercial Service officers a parity with senior economic officers in important U.S. foreign missions.

Catalog of U.S. Government Resources

Several U.S. Government agencies provide services that are or could be useful to U.S. exporters. Examples of these agencies are the Export-Import Bank, the Overseas Private Investment Corportion, the Small Business Administration, the Department of State, the Agriculture Department, and other agencies. Under Section 305 of the bill, the Commerce Department is directed to publish a catalog of these services to make the knowledge of these services more accessible to the exporting community. This will be particularly helpful to small and medium size businesses that do not have the contacts or resources to stay current with the various Federal export promotion programs. This catalog would be made available for sale through the Government Printing Office.

TITLE IV.—EXCHANGE RATES AND INTERNATIONAL ECONOMIC POLICY COORDINATION

HISTORY OF TITLE IV

The Subcommittee on International Finance and Monetary Policy held hearings on March 26 and April, 2, 1987 to review the impact of exchange rates on the U.S. balance of trade. The witnesses at the March 26 hearing were: David C. Mulford, Assistant Secretary for International Affairs, Department of the Treasury; Peter B. Kenen, professor of economics, Princeton University; C. Fred Bergsten, director, Institute for International Economics; Richard Cooper, professor of economics, Harvard University; Rimmer DeVries, vice president, Morgan Guaranty Trust Company of New York. The witnesses at the April 2 hearing were: Lawrence Fox, vice president for International Economic Affairs, National Association of Manufacturers; Henry Schechter, director, Office of Housing and Monetary Policy, AFL-CIO.

On May 1, 1987, a Committee Print of the U.S. Trade Enhancement Act of 1987 was circulated to the members of the Committee on Banking, Housing, and Urban Affairs. Title IV of the Committee Print dealt with the issues of exchange rates and international economic policy coordination. On May 19, 1987, the Committee marked up the Committee Print and adopted title IV with one amendment.

NATIONAL ECONOMIC POLICY IMBALANCES AND EXCHANGE RATES

In 1980, the U.S. trade deficit was $36 billion, but the current account was still in surplus at $2 billion. By 1983, the trade and current accounts were both negative—the trade and current account deficits had risen to $69 billion and $42 billion, respectively, and by 1986, to $170 billion and $141 billion.

The experience of the past five years—particularly prior to 1985—has led the Committee to take actions intended to make the Secretary of the Treasury more accountable for international financial matters and their effects on U.S. industries. The dollar rose sharply in value from 1980 to 1985—by fifty to eighty percent according to most measures. That rise in the dollar is generally believed to account for much of the deterioration of the U.S. trade and current account deficits.

As the dollar soared, the Treasury Department downplayed the injury to U.S. farms and factories and rejected proposals for corrective action. Only with new leadership in 1985 did the Department begin to acknowledge that the high dollar was a source of serious difficulties for U.S. industries. At the same time, it began to work with other industrialized nations to adopt policies to reduce trade and current account imbalances, through adjustment of exchange rates and macroeconomic policies.

The decline in the dollar over the past two years has decreased the competitive position of foreign nations significantly. As their trade surpluses decline, they will have to rely more heavily on the expansion of domestic demand to maintain economic growth. Japan in particular must allocate less of its resources to export industries and more to those industries satisfying domestic demand needs.

The United States at the same time must attempt to do precisely the reverse.

The United States must allocate more of its resources to export production and provide less stimulus to domestic consumption in order to improve its current account balances. In the trade surplus nations, more expansionary economic policies are needed to avoid the pain of recession and unemployment as those nations reallocate resources away from export sectors and into sectors producing to meet domestic demand.

Some nations have attempted to increase their exports in the face of a declining U.S. dollar by manipulating the value of their currencies relative to the dollar. These actions contribute to continued U.S. trade deficits and international economic imbalances. Nations that attempt to assure their export competitiveness through exchange rate manipulation must be encouraged to understand the risks associated with these practices and induced to let their exchange rates be determined by market forces.

ACTION RESPONSES

In an attempt to rectify the situation that let to the current international imbalances, title IV undertakes three critical initiatives.

First, section 404(b) of title IV directs the President to improve the quality of international economic coordination. In the Committee's judgment, there is clearly a need for the leading industrialized nations to coordinate their national economic policies in the interest of world economic growth and stability. The present degree of economic coordination, particularly among the United States, Japan, and West Germany, is, in the Committee's view, inadequate.

Second, section 404(c) directs the President to initiate negotiations with nations that manipulate their exchange rates to ensure that such nations regularly and promptly adjust the rate of exchange between their currencies and the dollar. The practice by some nations of manipulating the value of their currencies relative to the U.S. dollar to delay or prevent balance of payment adjustments continues to create serious competitive problems for U.S. industries.

And third, section 405 requires the Secretary of the Treasury to report annually to the Congress on the progress of the economic coordination discussions, currency market conditions, and the results of any negotiations with nations that manipulate the value of their currencies. The Federal Reserve is directed to include in its monetary policy report an analysis of the impact of the dollar's exchange rate on U.S. economic trends.

The Committee believes that every Administration should be held accountable for the exchange rate and the policies that underlie it. Requiring the Secretary to submitt and publicly defend a statement of policy on the current account and the exchange rate should help reach that goal.

It is the Committee's firm belief that these actions, implemented fully by the Administration, will contribute significantly to redressing the present enormous imbalances in the U.S. trade and current accounts.

EXCHANGE RATE MANIPULATION

The U.S. response to countries which manipulate the exchange rates of their currencies with respect to the dollar must be different from the response to nations which permit their currencies to "float" freely—that is, allow their exchange rates to be set in international financial markets. In the latter case, markets are permitted to equilibrate trade imbalances naturally over time and policies that shift the dollar in one direction tend to shift the exchange rates of all other currencies in the opposite direction. However, some nations manipulate the value of their currencies at a specific dollar value or range, by controlling foreign exchange transactions in their respective currencis or by other means simply to gain a competitive advantage.

Although the dollar has depreciated significantly against the floating currencies over the last two years, it has adjusted more sluggislhy against some major trade competitors that manipulate the value of their currencies to maintain competitiveness. The Committee is particularly concerned when such exchange rate manipulation results in both global current account surpluses and bilateral trade surpluses with the United States. For that reason, the Committee directs negotiations with such countries, bilaterally or in the International Monetary Fund, to regulary and promptly adjust their exchange rates.

REPORTING REQUIREMENTS

To enable the Congress to monitor the President's economic coordination efforts, title IV requires the Secretary of the Treasury to report in writing to the Senate and House Banking Committees by April 20th of each year on the conduct of international economic policy. It is the Committee's view that the Secretary of the Treasury should have responsibility for approving, announcing, and defending a statement of policy of the nation's international finances.

The Treasury Secretary's report is intended to assist Congress in (1) obtaining a full understanding of the present conflicts in the economic policies of the major industrialized nations, (2) developing a U.S. national economic policy that is consistent with an overall framework of international economic coordination, (3) monitoring closely the progress made by the President or his designees in negotiating an agreement coordinating national economic policies, (4) overseeing developments in exchange rates including situations involving manipulating currency values to the dollar to prevent effective balance of payments adjustments, (5) assessing the impact of the exchange rate of the dollar on the ability of the U.S. to maintain a sustainable balance in its current account and merchandise trade account, and (6) determining the size and composition of international capital flows, and the impact of such flows on exchange rates and trade flows. Of particular interst to the Committee are the results of any economic policy coordination agreement. If no agreement is reached, the Committee desires to be informed of the policy positions of the participants in the negotiations.

TITLE V.—INTERNATIONAL DEBT

HISTORY OF TITLE V

Since the onset of debt repayment problems among the less developed countries (LDC) in 1982, the Banking Committee has carefully monitored both the impact of the debt situation on bank safety and the role of U.S. banks in supporting recovery of indebted LDC economies. In 1983, the Committee held legislative hearings on the debt issue that examined a proposal to increase the level of resources in the International Monetary Fund (IMF) and legislation to require closer supervision of international lending by U.S. banks. This process culminated in passage of an increase in the U.S. quota at the IMF and the International Lending Supervision Act.

The Committee maintained continuing oversight of the debt issue in the 98th, 99th, and 100th Congresses. Bank safety remained a central issue, but the Committee's attention focused increasingly on restarting growth in the debtor economies as the key not only to the stability of the financial system, but to U.S. interests in restoring U.S. and world trade with important LDC markets and in preserving political stability in the countries themselves.

The Subcommittee on International Finance and Monetary Policy held hearings on international debt on March 26, April 1, April 2, and April 7, 1987 in preparation for the Banking Committee's consideration of legislation on the issue. The witnesses at the March 26 hearing were: David C. Mulford, Assistant Secretary for International Affairs, Department of the Treasury; Peter B. Kenen, professor of economics, Princeton University; C. Fred Bergsten, director, Institute for International Economics; Richard Cooper, professor of economics, Harvard University; Rimmer DeVries, vice president, Morgan Guaranty Trust Company of New York.

The witnesses at the April 1 hearing were: Jack D. Guenther, senior vice president, Citicorp; Charles L. Coltman III, executive vice president, Philadelphia National Bank; Salley Shelton-Colby, banking consultant; William D. Rogers, senior partner, Arnold and Porter; J.B.L. Pierce, vice president, Boeing Company; Dwayne O. Andreas, chief executive officer, Archer Daniels Midland Corporation; Bishop William Weigland, U.S. Catholic Conference.

The witnesses at the April 2 hearing were: Senator Bill Bradley (N.J.); Representative John J. LaFalce (N.Y.); Representative Charles E. Schumer (N.Y); Representative Bruce A. Morrison (Conn.); Rudiger Dornbusch, professor of economics, MIT; Karen Lissakers, adjunct professor, Columbia University School of International and Public Affairs; Andrew C. Quale, partner, Sidley and Austin; Allen I. Mendelowitz, Senior Associate Director, General Accounting Office; Robert R. Bench, Deputy Comptroller of the Currency; James J. Leisenring, Director of Research, Financial Accounting Standards Board; Thomas Keaveney, partner and National Director for Banking, Peat, Marwick, Mitchell and Company.

The witness at the April 7 hearing was Paul Volcker, Chairman, Federal Reserve Board.

On May 1, 1987, a Committee Print was circulated to the members of the Banking Committee. Title V of the Committee Print dealt with the issue of international debt. The Banking Committee marked up the Committee Print on May 19, 1987 and adopted title V with one amendment.

BACKGROUND

The Committee is increasingly concerned about the current status of the Third World debt situation. Since the "debt crisis" first appeared in 1982, a vast amount of attention has been devoted to the debt problem by private banking institutions, debtor governments, multilateral institutions, and the governments of the major creditor countries. While these efforts have averted a major crisis in the world financial system, there is not convincing evidence that policy to date has brought about an effective and long-term solution of the debt problem. Many Third World countries continue to have external debt burdens which are beyond their capacity to service, and many banking institutions have sufficiently large exposure to such debtors as to raise questions about their ability to survive a default or other major shock to the world financial system.

Recent events have only served to heighten the sense of urgency. The recent debt service moratorium by Brazil, following similar actions by Peru and Costa Rica and coinciding with increased tensions in negotiations between banks and other major debtors, suggests how tenuous the entire debt situation has become. Further, the decision by a number of major banks to increase significantly their reserves for losses on Third World debt appears to weaken prospects for a continuation of "concerted" lending by private commercial banks to debt problem countries.

The Committee believes that it is time for a new approach to the debt crisis. Since the debt problem is truly an international one, the appropriate solution to the debt problem must itself be international in scope. For that reason, the Committee's primary effort in the area of Third World debt is to establish a framework for international negotiations to work toward a new solution to the debt problem.

THIRD WORLD DEBT: EVOLUTION OF A CRISIS

The roots of today's crisis with Third World debt go back to the mid-1970's when a number of less-developed countries, particularly those in Latin America, significantly increased their external borrowings to avoid slowing their growth rates in response to the first and second "oil shocks". Although less-developed countries traditionally are net external borrowers, the size of the borrowings in the 1970's dwarfed all previous financial flows, and created an external debt burden which could not easily be serviced out of export income.

At the time, the extensive borrowing by debtor nations did not seem imprudent: world inflation was pushing commodity prices constantly higher, and with this came a dramatic rise in the export earnings of Third World commodity producers. This, combined with real interest rates which were low or even negative, made extensive external borrowing an attractive financial proposition for a great many countries.

Lending was also an attractive proposition for commercial banks, whose deposits from OPEC countries had grown enormously as the two oil shocks bolstered their foreign exchange surpluses. Willing lenders and willing borrowers in a climate of significant price inflation combined to produce the extraordinary run-up in external debt of the developing world.

Circumstances changed sharply in 1979, the year of the second oil shock, when the United States began to tighten monetary policy and drive world interest rates upward. Since much of the debt of the developing world was on a floating-rate basis, rising interest rates meant rising debt service obligations. At the same time, the slowdown in world growth helped to drive down commodity prices. Debtor nations were soon caught in a "price scissors", with their export earnings going down and their interest payments going up.

PHASE ONE OF THE DEBT CRISIS: MEXICO, THE IMF, AND FORCED AUSTERITY

The inevitable crisis created by falling export prices and rising interest rates eventually surfaced in the fall of 1982 when Mexico shocked the world by announcing that it was suspending payments on its outstanding debt. Mexico was only the tip of the iceberg, and the Mexican announcement touched off a near panic reaction by the world's commercial banks.

The banks reacted to the Mexican crisis by dramatically curtailing their lending to the developing world. Taken as a whole, the developing world increased its borrowing from private sources by $74 billion in 1981, the year before the Mexican crisis. In 1982, new borrowings fell to $48 billion, and they collapsed to $17 billion in 1983. The situation was far worse for the fifteen "heavily indebted countries" which saw net new lending of $56 billion 1981 fall to $29 billion in 1982, only to drop to a negative $2.6 billion in 1983.

This abrupt cessation of private lending set in motion a whole chain reaction of negative economic trends in the developing world. First, as new finance dried up, developing countries switched from being importers of financial resources to being exporters, as their combined payments of interest and principal on old loans significantly exceeded the new inflow of financial resources.

Finding the resources to finance this outward transfer required significant "adjustment" of the economies of debtor nations. Spending had to be curtailed sharply, and domestic savings increased, to provide the liquid assets to remit abroad. At the same time, debtor economies needed to be refocused on export production, since only exports produced the foreign exchange to pay debt service.

Generally supervised by the International Monetary Fund, these adjustments meant a drastic fall in living standards for the most of the residents of the debtor countries. Wages fell, subsidies were removed on key consumption items, and goods traditionally available on local markets disappeared as production was refocused on exports. While the cut in consumption standards was painful for the residents of the debtor countries, the debt crisis also caused more serious dislocaions in world trade and in the ability of debtor countries to grow in the future. Between 1981 and 1984, the trade balance of Latin America moved from a deficit of $4 billion to a surplus of $38 billion, as debtor countries were forced to adjust their economies to makeup for the collapse of foreign financing. But their increased export production only served to worsen the glut on world markets, depressing commodity prices for all exporters.

On the domestic side, the greatest problem of the IMF strategy was that it led to cuts in domestic investment. Since the onset of the debt crisis, countries with debt service problems have been asked to export financial resources amounting to over 4 percent of their GNP. These resources had to be withdrawn from other potential uses in the economy, to be sent abroad to satisfy their creditors, and the loss of domestic resources translated directly into lower rates of domestic growth. Since the debt crisis, capital investment as a share of GDP in the developing world has fallen by 5 percent, but it has dropped a staggering 27 percent in those countries where debt servicing problems have most dramatically shifted the resource transfer equation.

To its credit, the IMF recognized that there were clear political and economic limits to its austerity strategy, and consequently sought to increase the external resources available to debtor countries ot help manage the adjustment process.

To provide the needed external resources, the IMF worked to persuade the private banks to provide new loans in the form of "concerted" lending packages. Plans were developed in consultation with the IMF to determine precisely how much new extenal finance was needed to maintain some level of economic activity in the debtor nations, and then the commercial banks which already had loan exposure to the country were asked to contribute new lending in proportion to their existing exposure. These new loan packages were generally accompanied by a rescheduling of old debt, another tacit recognition by all the parties that countries simply could not affort to repay principal on their old debt.

The combination of reschedulings, "concerted lending" and IMF-supported policy change in the debtor countries was sufficient to prevent a major default or other crisis in the world financial system, but it was clearly inadequate to meet the needs of either the debtor countries for growth or the world economy for expansion of export markets. Real GDP growth in the most heavily indebted countries was −0.4 percent in 1982, −3.4 percent in 1983 and a modest 2.2 percent in 1984. Import volumes in the same countries fell 16.7 percent in 1982, 21.2 percent in 1983 and 2.9 percent in 1984.

PHASE TWO OF THE DEBT CRISIS: THE BAKER PLAN

World recognition that the debtor countries were growing too slowly and importing too little grew steadily during 1984 and 1985, and this recognition culminated in the announcement of the "Baker Plan" in September of 1985. The plan crafted by Treasury Secretary Baker called for faster growth in the debtor nations and an increased commitment by governments, multinational financial institutions and private banks to provide the additional finacne needed to sustain growth and adjustment. The Baker Plan called for a three year program to increase external lending to the debt-problem countries by some $9 billion a year.

The shift of emphasis from austerity in growth was a welcome change in policy for dealing with the debt problem, but the Baker Plan raised questions about whether the new effort would be sufficient.

The sum mentioned in the Baker Plan were modest in comparison with the size of the problem. At present, the fifteen countries mentioned in the Baker Plan are paying roughly $40 billion per year in interest payments on their old debt, and receiving roughly $10 billion in new capital flows from official donors and private investors. This means net outflow of financial resources of some $30 billion per year. The Baker Plan would reduce the yearly outflow by only $9 billion, leaving the poor countries as substantial exporters of capital at a time when more domestic investment is needed for growth.

A more difficult problem concerned the nature of the new financing envisioned by the plan. The lion's share of funds was to come from private commercial banks in the form of new lending, at a time when countries were already having difficulties servicing their existing debt. Between 1983 and 1986, the debt-to-export ratio and the interest payment-to-export ratio for the fifteen countries mentioned in the Baker Plan actually deteriorated rather than improved. Those ratios would move even further away from commercial "creditworthiness" if additional debt were added. This raises questions about both the willingness of banks to extend the loans and the wisdom of asking already indebted countries to go further into debt.

The issue of bank willingness to lend has assumed significantly greater importance in the past few weeks, with the announcement by several major banks of large increases in their reserves for loan losses on Third World debt. The decision by banks to reserve represents a judgment by senior bank managers that losses are likely on these loans, and that they will in all probability not be repaid in full. While bank self-interest in preventing a default may sustain some modest new lending, it is highly unlikely that commecial banks will make available even the volume of new lending envisioned in the Baker Plan, much less the larger sums required to truly restart the growth process in the Third World.

PHASE THREE OF THE DEBT CRISIS: THE NEED FOR NEW POLICIES

The Committee believes that the Third World debt crisis is now moving into a third phase, one which requires new policy initiatives by both industrialized and developing countries if the world is to avoid a destabilizing economic crisis in the debtor countries. The Committee believes that important U.S. interests are at stake in the Third World, and that the absence of a credible long-run solution to the debt problem is damaging to those interest.

The United States has an interest in the maintenance of democratic institutions throughout the world, and in the strengthening of democracy in debtor countries which have recently passed from authoritarian to democratic rule. Democracy cannot long survive the strains of a crippled economy with growth below that required to increase even modestly the per capita income of a nation.

The United States has an important economic interest in the resumption of U.S. exports to large debtor countries. Latin America has traditionally been a strong natural market for American exports, but import growth can accelerate in these countries only if some long-term solution is found to their needs for external finance.

The United States also has an important interest in the maintenance of growth in the trading system. Policies to ease the demand constraint posed by excessive debt in the Third World must be an essential part of any strategy for stimulating global growth.

STEPS TOWARD A LONG-TERM SOLUTION

The Committee believes that pursuit of these goals requires new policies designed to broaden the range of options available to deal with the debt problem. Options currently available include: 1) encouraging economic reform in debtor countries through the IMF or other mechanisms; 2) encouraging banks to provide additional "concerted lending" to help countries grow and adjust; 3) encouraging private investors to contribute toward financing Third World economic growth through direct investment and debt-for-equity swaps.

What is missing from the current range of options is any mechanism to significantly restructure the existing debt of many of these countries in such a way as to permit resumption of economic growth while facilitating debt service obligations. The lack of any mechanism for effecting this type of debt restructuring stands as a major obstacle to a long-term solution to the debt problem.

What is needed at this point is a mechanism to achieve these objectives. Toward this end, the Committee has defined a set of objectives and directives to the Secretary of the Treasury to initiate discussions with other governments toward the establishment of an International Debt Management Authority.

SUBTITLE B: THE INTERNATIONAL DEBT MANAGEMENT AUTHORITY

The Committee believes that an appropriate mechanism for addressing the debt service issue would be the creation of a new multilateral entity to purchase, and the restructure, the debt of some Third World countries from the commercial banks.

Restructuring would improve the creditworthiness of the debtor countries in three ways. First, the facility would purchase loans at a discount from their face value, and then pass the discount along to the debtor countries. Banks would have to recognize losses on these loans sales, but in return would get increased liquidity for new lending and relief from the expense, complexity, and dangers of future debt negotiations. Second, the facility would transform the short-maturity bank loans to the longer term lending needed for development, thereby reducing the annual debt service burden. Third, the facility would charge lower rates on the remaining loans because it would not be trying to earn profits and it would obtain funds at the lowest market rates.

The Committee has emphasized an international facility because of the importance which the Committee attaches to ensuring the participation of other industrialized countries in the creation of such an entity. The debt problem is truly an international one, with U.S. domestic banks accounting for only about one-third of the total outstanding debt, and should be addressed on an international basis.

OBJECTIVES OF DISCUSSIONS

The Committee directs the Secretary of the Treasury to begin discussions on the creation of a debt management institution with whatever countries he determines are appropriate. The Committee intends that any proposals which emerge from these discussions should reflect the following objectives:

(1) that industrialized countries should cooperate in supporting such an entity, and that greater support should be expected from countries with strong current account surpluses;

(2) that any intermediary should have close working relationships with both the IMF and the World Bank;

(3) that any intermediary should be designed to operate as a self-supporting entity, requiring no routine appropriation of resources from any member government;

(4) that any intermediary should have a defined termination date and a clear proposal for the restoration of creditworthiness to debtor countries within this timeframe.

The Committee believes that countries which enjoy substantial current account surpluses should be called upon to play a large role in the establishment of any new debt management authority. The world economy is suffering from slow growth and rising international tensions in large part because of the huge surpluses which have been accumulated by a number of trading nations. The financial power which these surpluses represents needs to be redeployed to stimulate growth elsewhere in the world economy if we are to avert a dangerous declining spiral in world trade.

The Committee believes that a close working relationship with both the IMF and the World Bank will be essential to the success of any debt intermediary. The Committee recognizes that policy reform in the debtor nations must continue, and that any restructuring of existing external debt obligations must be accompanied by a clear willingness by the debtors to improve their use of external resources. Close collaboration between the IMF, the World Bank and any such entity will be essential to furthering this goal of policy reform.

The Committee believes that any debt intermediary should be designed to operate as a self-supporting entity, and that any intermediary proposal arising out of these negotiations would have a clearly defined timeframe.

ACTIONS TO FACILITATE THE CREATION OF THE FACILITY

The Committee believes that the creation of a new intermediary institution to manage the debt problem is a task which must be approached with a sense of urgency by all nations.

To contribute to rapid progress on this issue, the Committee has directed the Secretary of the Treasury to explore all potential resources already available which could be committed to the task of starting and funding a debt intermediary. In particular, the Committee asks the Secretary to consider whether a portion of the IMF's gold stock, valued at approximately $40 billion, could be used as collateral to back the initial debt offerings of a potential facility. If the IMF gold or other idle resources could be applied to back the initial capitalization of an intermediary, it should be possible to move forward with such a proposal without delay.

REDUCING CAPITAL FLIGHT

The Committee notes that the resources transfer equation for many debtor countries has been significantly worsened by the exodus of "flight capital" from debtor countries. While estimates vary about the size of the problem, there is little disagreement that substantial sums of money are controlled by residents of debtor countries but placed outside of their countries in bank accounts, real estate or other forms of investment.

For this reason, the Committee calls on the United States Executive Director of the International Monetary Fund to initiate discussions on policy proposals for both development and developing countries which would reduce the level of outward capital flight in the debtor nations.

SUBTITLE C—REGULATORY PROVISIONS AFFECTING INTERNATIONAL DEBT

Today's debt crisis is not only a threat to growth in the developing world but also to financial stability in the industrialized world. For this reason, bank regulatory policy needs to treat Third World debt differently from domestic debt. The Committee believes that the agencies responsible for the regulation of financial institutions must recognize the risks inherent in lending to over-extended Third World countries and work to ensure that banks have an adequate cushion of capital and reserves to protect bank depositors in the event of a payment crisis in the Third World.

But the Committee also believes that regulatory policy should not discourage banks from developing new solutions for the financial problems of their Third World clients. Steps to ease the current payments burden borne the Third World borrowers can, in some circumstances, improve the possibility that loans to that borrower will be repaid in full at some later date. It would be poor use of regulatory discretion to discourage banks from exploring such avenues.

The regulatory provisions of this bill focus on the role of U.S. commercial banks and bank regulators in resolving the debt crisis, and restate the Committee's two key concerns. First, U.S banks must continue taking the steps necessary to ensure their safety and soundness. Second, in their continuing financial support of heavily indebted countries, bansk must have the flexibility to pursue a broader range of financial options, extending beyond new lending alone to restructuring the terms and conditions of their existing portfolio of loans.

LEGISLATIVE ACTIONS

Facilitation of Debt-for-Equity Exchange.—One financial option to help reduce the debt burden of the developing countries is debt-for-equity exchanges or "swaps". Debt-equity swaps involve conversion of a fixed or floating-rate loan made to an LDC government or company into an equity position in the company or country involved. While debt-equity conversions alone will not solve the debt problem, the Committee believes that property structured debt-equity programs may be of benefit to debtors and investors alike.

In recognition of the supply and demand constraints facing debt-equity conversion programs and potential regulatory impediments to a broader range of debt management mechanisms, the Committee endorsed two provisions designed to encourage action by host countries, creditor banks, and U.S. bank regulatory agencies to facilitate debt-equity swaps.

In section 522(a) of the bill, the Committee directs the Federal bank regulatory agencies to study potential accounting and regulatory constraints to debt-equity conversions and to report back to the Congress on them by January 15, 1988 including recommendations for legislative changes. While in its markup of legislation, the Committee decided against specific amendments to alter regulations on swaps into non-banking activities, Section 522(a) is intended to ensure that this issue and other accounting and regulatory questions are fully considered by the regulators.

Section 522(b) addresses supply constraints to debt-equity programs. It directs the Secretary of the Treasury to instruct the U.S. Executive at the Third World Bank to initiate discussions with other directors of the Bank on the appropriate role for the World Bank and the International Finance Corporation (IFC) in supporting debt-equity swaps, and to propose that the World Bank and the IFC more actively promote the development of domestic capital markets in developing countries, encourage improvements in LDC investment policies, and help facilitate debt-equity conversions.

REGULATORY STUDY

Section 523 directs the Secretary of the Treasury and the appropriate Federal regulatory agencies to prepare and submit a report on current regulatory practice in regard to Third World debt. The report is designed to identify regulatory obstacles which prevent or inhibit banks in the development of creative new devices for restructuring Third World debt obligations.

In this report, the Committee desires to have the regulatory agencies identify any policies and practices by either bank accountants and auditors, or the bank regulatory authorities themselves, which inhibit banks from developing on a voluntary basis, loan restructurings which involve reductions in current debt payments by borrowers. In this regard, examination of the applicability of Financial Accounting Standards Board Standard No. 15 to Third World debt restructurings might be appropriate.

TITLE VI.—NATIONAL TREATMENT OF FINANCIAL INSTITUTIONS

BANKS AND BANK HOLDING COMPANIES

Background.—The Committee has been concerned with issues of national treatment for more than a decade. The guiding principle of the International Banking Act of 1978 was to provide such treatment to foreign banking organizations in the United States: to accord them the same competitive opportunities as U.S. banking organizations enjoy. As described in the Treasury Department's Report to Congress on Foreign Government Treatment of U.S. Commercial Banking Organizations (1979) (the original National Treatment Study), national treatment "afford(s) foreign banks equality of competitive opportunity vis-a-vis domestic institutions in similar circumstances." It "entails a pragmatic impact- or effects-oriented test for assessing the overall legal and regulatory climate affecting foreign banks in a given country. The test is met if foreign banks are allowed to compete on essentially equal terms with domestic institutions in the host country, even if some specific regulations or requirements applied to foreign banks differ from those affecting domestic banks."

The Committee's report on the International Banking Act noted that the United States "has more than abided by the principle of national treatment for foreign banks operating here," whereas "our domestic banks operating abroad have not always received equal treatment in foreign countries with their host country competitors." The Committee declared that "the United States, in light of the substantial privileges enjoyed by foreign banks in the United States should seek to secure national treatment for our banks abroad as well." As an initial step toward that goal, section 9 of the International Banking Act directed the Secretary of the Treasury to report on the extent to which U.S. banks "are denied, whether by law or practice, national treatment in conducting banking operations in foreign countries," and on "the efforts undertaken by the United States to eliminate any [such discriminatory] laws or practices".

The 1979 National Treatment Study, prepared pursuant to that directive, detailed extensive discrimination against U.S. banking organizations abroad.

In 1983, Senator Garn introduced S. 2193, which required the Comptroller of the Currency, when acting on an application by a foreign bank to establish a Federal branch or agency, to consider the treatment of U.S. banks in the applicant's home country. The Committee held hearings on that bill on September 26, 1984. Witnesses at the hearing included the Honorable Donald T. Regan, Secretary of the Treasury; Mr. Peter Howell, vice president of Citibank, N.A.; and Mr. Robert P. Williamson, president of the Bankers' Association for Foreign Trade.

The 1984 and 1986 Updates to the National Treatment Study, prepared at the request of Senator Garn, demonstrated that many countries continue to discriminate against U.S. banking organizations.

Committee Action.—The Committee adopted section 601 to help end such discrimination. Section 601 permits the Federal banking agencies, with the prior approval of the President, to deny applications filed by banking organizations from countries that do not accord national treatment to U.S. banking organizations. That authority, although purely discretionary, strengthens the hand of the United States in negotiating to end discrimination against U.S. banking organizations abroad. The requirement of prior Presidential approval ensures that any exercise of that authority will be consistent with overall foreign policy.

Although the Committee hopes that discrimination by foreign countries against U.S. banking organizations can be ended without exercising the authority provided in section 601, the Committee intends that the Treasury and the Federal banking agencies vigorously seek to end such discrimination.

PRIMARY DEALERS

Background.—The Committee has also been concerned about discrimination against U.S. companies in the underwriting and distribution of foreign government securities. The 1986 Update to the National Treatment Study found that in Japan:

> Foreign firms are allocated a very small proportion of bonds in the government bond underwriting syndicate. * * * Allocations are based on a syndicate member's size of operations and experience only in Japan. As a result, even large foreign securities firms and banks with extensive experience in government bond markets receive an extremely small fraction of each issue (less than 0.1 percent each), which is comparable to those often allocated to small Japanese securities firms and the regional banks.

In response to that and other discriminatory practices in Japan, Representative Charles E. Schumer introduced legislation (H.R. 1463) to limit the designation of foreign-controlled companies as primary dealers in U.S. Government securities. That proposal is now section 428 of H.R. 3, as passed by the House of Representatives on April 30, 1987.

Primary dealers are those dealers with which the Federal Reserve System deals directly when buying and selling U.S. Government securities in the course of its open-market operations. BankAmerica Corporation, 73 Fed. Reserve Bull. 361, 362 n.2 (1987). Primary dealers also make a secondary market in such securities and are major bidders at Treasury auctions.

Committee Action.—Effective two years after enactment, section 602 prohibits the Federal Reserve System from designating, or continuing any prior designation of, any person of a foreign country (other than Canada or Israel) as a primary dealer unless the foreign country in question accords U.S. companies national treatment in the underwriting and distribution of its government securities. But the Federal Reserve is not required to rescind the designation of a company that became a primary dealer before being acquired by a person of a foreign country and that was acquired by that person before January 1, 1987.

Section 602 differs from section 428 of H.R. 3 in being based on national treatment rather than reciprocity; in containing a grandfather provision for previously designated primary dealers acquired by persons of a foreign country before January 1, 1987; in containing exceptions for Canada and Israel; and in taking effect two years, rather than six months, after enactment.

The objective of both proposals is to encourage foreign countries to end discrimination against U.S. companies in the underwriting and distribution of government securities, rather than to exclude foreign companies from the United States. The two-year delay in the effective date of section 602 furthers that objective by giving foreign countries ample time to come into full compliance with the standard of national treatment. The Committee is concerned that the six-month delay in H.R. 3 is so unrealistically short that it undercuts the incentive for a foreign country to make major reforms.

The Committee expects that during the two years before section 602 takes effect, the Federal Reserve will use its current authority over primary dealers to encourage countries that discriminate against U.S. companies to move expeditiously toward according national treatment. As Mr. E. Gerald Corrigan, president of the Federal Reserve Bank of New York, declared in a December 11, 1986 letter to Representative Schumer:

> In announcing the decisions we have reached (including the designation as primary dealers of two U.S. subsidiaries of Japanese securities companies), we are making clear our expectations that naming Japanese-owned firms as primary dealers must be viewed as a catalyst for further significant actions such as these with respect to the Japanese market in the period ahead. Thus, our decisions reflect our commitment to the policy of national treatment, but a continuation of that commitment must depend on a steady flow of complementary policy actions in key markets abroad. Absent that flow of actions, we would see little scope for further action on our part and might very well have to rethink actions already taken.

TITLE VII.—AMENDMENTS TO THE FOREIGN CORRUPT PRACTICES ACT (FCPA)

HISTORY OF TITLE VII

The precursor of this title of the Trade Enhancement Act of 1987 was first introduced in the 97th Congress by Senator Chafee on March 12, 1981 as S. 708. Joint hearings on that bill were held before the Senate Banking Committee's Subcommittee on Securities and its Subcommittee on International Finance and Monetary Policy on May 20 and 21, June 16, and on July 23 and 24, 1981. On September 16, 1981, the Committee reported S. 708 after amendment by a vote of 11 to 4. On November 23, 1981, the full Senate passed S. 708 on a voice after it was further amended on the floor. The bill never became law as the House did not act upon the Senate proposed amendments to the FCPA.

On February 3, 1983, Senators Heinz, Chafee, Garn and D'Amato introduced S. 414 (in the same form as S. 708 which passed the Senate in 1981). A joint hearing on that bill was held by the Subcommittee on Securities and the Subcommittee on International Finance and Monetary Policy on February 24, 1983. The full Committee agreed by a poll vote of 17 yeas to 1 nay to report S. 414 on May 25, 1983. That bill was never considered by the full Senate in the 98th Congress.

On February 7, 1985, Senators Heinz, Chafee, Garn and D'Amato introduced S. 430 (in the same form as S. 414 and S. 708). A joint hearing on the bill was held by the Subcommittee on International

Finance and Monetary Policy and the Subcommittee on Securities on June 10, 1986. Testimony was received from Malcolm Baldrige, Secretary of Commerce; Edward H. Fleischman, Commissioner of the Securities and Exchange Commission; John C. Keeney, Deputy Assistant Attorney General, Criminal Division, Department of Justice; Calman J. Cohen, vice president, Emergency Committee for American Trade; Allen B. Green, partner, McKenna, Connor and Cuneo, representing the public contract law section of the American Bar Association; and Arthur F. Matthews, partner, Wilmer, Cutler and Pickering.

On September 17, 1986, the full Banking Committee agreed to report S. 430 by a vote of 11 yeas to 3 nays. S. 430 was not considered by the full Senate in the 99th Congress.

On March 3, 1987, Senator Garn introduced S.651, an Administration drafted bill to amend the Foreign Corrupt Practices Act (FCPA). While similar to the previous bills (S. 708, S. 414, and S. 430), there were changes in the bill made in response to testimony by the Justice Department at the June 10, 1986 hearing. For example, the new bill retained agents within the FCPA's coverage and certain of the facilitating and other payment exceptions from the prohibition on bribery were narrowed. The Committee did not hold hearings on the new bill in the 100th Congress. The provisions of S.651 were offered by Senator Chafee as an amendment to Committee Print No. 1 of the Trade Enhancement Act of 1987. After the amendment was offered and prior to the May 19 markup of the Committee Print, the Chafee amendment was modified in regard to various points raised by Senator Proxmire. During the May 19 markup the Chafee amendment was further modified by two second degree amendments. It was reported out on a voice vote as title VII of the Committee's trade bill which will be taken up on the Senate floor in conjunction with the full Senate's consideration of omnibus trade legislation.

PURPOSES OF THE LEGISLATION

The amendments to the FCPA in this title are intended to clarify the meaning of various provisions of that Act and to make clear Congress' intent with regard to such provisions. To do this, the amendments clarify the language governing the responsibility of corporations for the activities of their agents so as to reduce unnecessary concerns about potential criminal liability among exporters. The amendments also make clear that compliance with the FCPA's books and records, and accounting provisions does not require excessive paperwork and that insignificant and inadvertent errors in complying with those provisions are not subject to criminal penalties. In making these changes, the bill expressly adopts the view that the principal goals of the FCPA—i.e. preventing the use of corporate funds for corrupt purposes, and outlawing bribery by United States corporations of foreign officials to win sales—are important objectives which should continue to be pursued. The Committee believes that the amendments to the FCPA in this title will not interfere with attaining these objectives and will lessen concerns, expressed by same, that the present law act as a disincentive to U.S. exporters.

BACKGROUND ON THE FCPA

The FCPA was enacted in 1977 in response to disclosures of questionable and in some cases illegal foreign payments made by U.S. companies to foreign officials in order to secure export business.

Beginning in 1973, as a result of the findings of the Watergate Special Prosecutor, it became clear that many corporations had made substantial, illegal contributions during the 1972 Presidential election campaign. The secret contributions were made possible by off-the-books slush funds being maintained by many of America's largest corporations. Subsequent SEC investigations into such corporate slush funds and voluntary disclosures by corporations revealed that instances of undisclosed, questionable or illegal corporate payments, both domestic and foreign, were widespread. These revelations demonstrated that there were substantial shortcomings in our Government's ability to police the illegal use of corporate funds by the management of our corporations. In fact, it was revealed that top management often did not know how their own corporation's funds were being used. Boards of directors of corporations often pleaded ignorance about the misuse of corporate funds entrusted to them by public shareholders.

The SEC's formal report to Congress in 1976 on questionable payments stated:

> The most devastating disclosure that we have uncovered in our recent experience with illegal or questionable payments have been the fact that, and the extent to which, some companies have falsified entries on their own books and records.

The SEC subsequently stated that illegal payments and falsifications of books were made possible because internal corporate accounting controls were ineffective or easily subverted.

Follow up investigations in 1976 and 1977 revealed that American corporations not only made questionable payments at home, but were also doing so abroad to gain business. During hearings on these matters, Congress concluded that corrupt payments to foreign officials caused serious damage to America's national interests in critical areas of the world.

The question before the Congress in 1977 was whether it should permit some dishonest corporations to harm U.S. foreign policy interests in their zeal for sales and profits. It answered, "No" unanimously. It was the view of Congress that bribes are bad for business because they distort free markets. Goods should be sold on the basis of price, quality, and service, not on the basis of bribes. It was also the view of Congress that a strong antibribery statute could help U.S. corporations resist corrupt demands, and that bribes undermined confidence in America's integrity, corrupted other governments, and created severe foreign policy problems for the United States. Congress, in 1977, found that bribes were illegal in most countries and were not necessary to do business abroad. So the assertion that bribes were a way of life in some countries—did not mean the people of those countries wanted such behavior to be the norm. Just as Americans do not want foreign corporations bribing our officials—so do people in other countries resent the use of bribery for foreign corporations in their countries. The amendments to the FCPA in this title do not change Congress' previous conclusions about the need to prohibit corporate bribery as a means to win sales.

PROVISIONS OF PRESENT LAW

Congress attempted to prevent corporate bribery of foreign officials by three basic provisions of the FCPA:

1. Accounting Controls

(a) Integrity of Books and Records.—The FCPA requires firms with securities registered with the Securities and Exchange Commission (SEC) to keep detailed books, records, and accounts accurately reflecting corporate payments and transactions.

Section 102 of the FCPA amended section 13(b) of the Securities Exchange Act of 1934, codified at 15 U.S.C. 78q (b), adding subparagraph (b)(2)(A) to require firms regulated by the SEC to "make and keep books, records, and accounts, which, in reasonable detail, accurately and farily reflect the transactions and disposition of the assets" of the firm. This provision thus prohibited the "disguising" of questionable payments made to persons overseas and prohibited secret slush funds; that is, "inaccurate books, off-the-book accounts and related practices" (SEC Release No. 14478, Feb. 16, 1978). Penalties for violations of the books and records requirements are those penalties applicable generally to violations of other provisions of the Securities Exchange Act. In addition to civil injunctive relief that may be sought by the SEC (15 U.S.C. 78u), criminal penalties of fines up to $10,000, later raised to $100,000 or imprisonment of up to 5 years or both may be imposed (15 U.S.C. 78ff).

(b) Internal Accounting Controls.—Firms with securities registered with the SEC are required to institute and maintain an internal accounting control system to assure management's control, authority, and responsibility over the firm's assets.

Section 102 of the FCPA further amended section 13b of the Securities Exchange Act of 1934 by adding sub-paragraph (b)(2)(B) that requires firms regulated by the SEC to design and implement an adquate system of internal accounting controls "to assure, among other things, that the assets of the issuer are used for proper corporate purposes" (S. Rept. 95-114, 95th Congress, 1st Sess., p. 7). This section requires the maintenance of an internal accounting control system to assure that transactions of the firm are executed, and access to the firm's assets is permitted only "in accordance with management's general or specific authorization"; and to assure that transactions are recorded and identified in conformance with generaly accepted accounting standards. Penalties for violations of this provision are the same as those for the books and records provision.

2. Criminalization of Foreign Bribery

The FCPA specifically prohibits domestic firms, whether registered with the SEC or not, from corruptly bribing a foreign official, a foreign political party, party official, or candidate for the purpose of obtaining or maintaining business.

(a) Direct Bribes.—Sections 103 and 104 of the FCPA make criminal the act of corporate bribery in foreign countries. Under these sections, criminal penalties are provided for any firm regulated by the SEC or for any other domestic concern which uses the mails or interstate commerce "corruptly" in furtherance of an offer or payment of money or anything of value to a "foreign official" or to a political party, party officials, or candidate for foreign political office for the purpose of influencing such person in his decision making or in the use of his influence to affect governmental decisions to assist the firm in obtaining or retaining business. (See section 103 of the FCPA, amending the Securities Exchange Act of 1934 by adding section 30A to the 1934 Act, 15 U.S.C. 78dd-1; and section 104 of the FCPA, adding 15 U.S.C. 78dd-2.)

(b) Indirect Bribes and "Reason to Know".—In addition to prohibiting such bribes directly by a firm or by any of its employees, officers, agents, or directors acting on its behalf, the Act also prohibits the payment of money to any person by a firm if the firm knew or had reason to know that a portion or all of such payment was to be used to bribe a foreign official for his influence in obtaining or retaining business. These provisions place an affirmative responsibility on the corporation to exercise control over its officers, directors, or employees and to take steps to assure that its overseas agents will not use corporate assets or payments made to them for the purpose of bribing foreign officials. (See S.Rept 95-114, p.l.)

(c) Exceptions to Bribery Prohibitions.—Not all payments to employees of foreign governments were contemplated by Congress to be considered illegal bribes under the statute. First, the definition of "foreign official" within the Act excludes those employees of a foreign government "whose duties are essentially ministerial or clerical" (sections 103(b) and 104(d)(1) of FCPA of 1977). Second, the legislative history of the Act states specifically that the Act was not intended to cover minor payments such as "payments for expediting shipments through customs or placing a transatlantic telephone call, securing required permits, or obtaining adequate police protection, transactions which may involve even the proper performance of duties" (S.Rept. 95-114, p.10).

(d) Penalties.—Penalties for violations of the bribery provisions of the Act include fines for the firm or corporation of up to $1,000,000 for the firm or corporation and fines of up to $10,000 or imprisonment of up to 5 years or both for individuals. The Attorney General is further authorized to seek injunctive relief against a domestic firm or individual when it appears that it is engaged or is about to engage in a violation of the bribery provisions.

3. Enforcement.

Two Federal agencies are involved in the enforcement and administration of the FCPA. The recordkeeping and accounting controls provisions of the FCPA, requiring fair and accurate accounting of corporate transactions and expenditures by U.S. publicly-held companies, are under the authority of the SEC. The SEC also has civil injunctive authority to enforce the prohibitions against foreign bribery by U.S. publicly-held companies. The enforcement of the criminal penalties for corporate "bribery" of foreign officials are primarily under the prosecutorial authority of the Department of Justice which also has the authority to bring civil actions against domestic concerns whose securities are not registered with the SEC.

NEED FOR AMENDMENTS

The FCPA is a good law. The evidence since enactment a decade ago shows that the FCPA has been effective and that most U.S. companies have not engaged in slush fund bookkeeping nor used bribery as a way to win sales abroad. This success is applauded by all members of the Banking Committee. Almost from the enactment of the present FCPA, however, certain of its provisions have been criticized for vagueness and for creating unnecessary paperwork burdens and concerns among exporters over their liabilities for unauthorized acts of their agents. U.S. exporters have stated that such concerns have had a chilling effect on their legislative efforts to compete for sales abroad resulting in lost business opportunities. The Committee acted to amend the present law to clarify its provisions and alleviate such burdens and concerns while not weakening its effectiveness in stemming bribery.

AMENDMENTS TO BOOKS AND RECORDS AND ACCOUNTING CONTROLS

1. *Insignificant or Inadvertent Errors.*—An SEC witness told the Committee that many commentators expressed concerns that the accounting provisions of the FCPA expose persons to criminal liability based on technical or insignificant errors in corporate records or weakness in corporate internal accounting controls. To quiet such concerns, the SEC, in 1981, issued a Statement of Policy expressing its view that the accounting provisions do not mandate exactitude in recordkeeping or an ideal system of internal accounting controls. At the June 1986 hearing, SEC Commissioner Edward Fleischman noted that the SEC, in its 1981 policy statement, recognized that the accounting provisions must be—

> * * * limited by a concept of reasonableness that tolerates certain deviations from the ideal and contemplates a cost-benefit analysis. The Commission also stated that the principal purpose of the accounting provisions is to reach knowing or reckless conduct.
>
> In its enforcement efforts under the accounting provisions of the FCPA, the Commission has adhered to its 1981 Statement of Policy. The cases have not involved insignificant or technical infractions, nor have individuals been charged with inadvertent conduct.

To ensure that the SEC would not bring criminal penalties for inadvertent or insignificant errors in books and records, or inadvertent violations of accounting controls, business groups and the Administration requested that the law itself be amended to codify the Commission's stated enforcement policy. The amendments reported by the Committee accomplish this by providing that criminal penalties shall not be imposed for failing to comply with the FCPA's books and records or accounting control provisions (See section 703.) The Committee bill, however, specifically provides that "No person shall knowingly circumvent a system of internal accounting control or knowingly falsify books, records or accounts established or kept pursuant ot the provisions of the FCPA." (Also at section 703.) This provision is meant to ensure that acts of commission or omission in keeping books or records or administering accounting controls would be subject to criminal penalties if their purpose was to falsify books, records or accounts, or to circumvent the accounting controls set forth in the FCPA. This would include the deliberate falsification of books and records and other conduct calculated to evade the internal accounting controls requirement.

2. Cost/Benefit Clarification.—Some businesses have expressed concerns that the book and records and accounting systems requirements are burdensome because they have caused businesses to incur costs substantially in excess of the benefits derived from the expenditures. While the FCPA does not itself address the matter, the 1977 Committee Report on the FCPA stated "The Committee recognizes that management must necessarily estimate and evaluate the cost-benefit relationships of the steps to be taken under the books and records and accounting requirements." To make this point absolutely clear, the amendments define the terms "reasonable detail" and "reasonable assurances" in the present law to "mean such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs, having in mind a comparison between benefits to be obtained and cost to be incurred in obtaining such benefits." (Also at section 703.) The Committee believes this amendment, while not carrying enforcement practices under current law, will alleviate some corporate concerns which have led them to incur unnecessary costs in complying with the requirements.

3. Records of Subsidiaries.—The FCPA is silent on the issue of the legal responsibility of an issuer for compliance by subsidiaries with the accounting requirements. Conflicting views have been expressed concerning the nature of this responsibility, particularly with respect to subsidiaries in which an issuer does not own a majority interest.

Section 703 of the Committee's amendments provide that such an issuer's responsibility is discharged where the issuer makes a good faith effort to cause the subsidiary to comply with the amended requirements of section 13(b)(2). This approach is based upon the recognition that it is not realistic to expect a minority owner to exert a disproportionate influence over the accounting practices of a subsidiary's internal accounting controls. The amount of influence which an issuer may exercise necessarily varies from case-by-case, depending on a variety of factors. While the relative degree of ownership is obviously one factor bearing on the issuer's influence, other factors may also be important.

The good faith requirement approved by the Committee is intended to be consistent with other amendments to the FCPA incorporated in this title, in that the issuer's conduct, rather than that of persons or entities not subject to the issuer's control, will determine whether the issuer is deemed to have violated the accounting controls provisions.

AMENDMENTS TO BRIBERY PROVISIONS

1. Enforcement Consolidation.—Under the current law the SEC has authority for enforcing against "issuers" the civil remedies for violation of the anti-bribery provisions. The Justice Department enforces against "issuers" the criminal penalties for violations of the anti-bribery provisions and the civil and criminal remedies for such violations against "domestic concerns". Such a division of enforcement responsibility can lead to the application of different standards of enforcement to public companies and to other persons. Therefore, the amendments adopted by the Banking Committee give the Justice Department all jurisdiction with respect to civil and criminal enforcement of the anti-bribery provisions of the FCPA. The amendment provide, however, that the SEC may transmit evidence it has of any violations of the anti-bribery provisions to the Justice Department, and that Justice must report annually to Congress on the disposition of such referrals. (See section 704.) The Committee expects that the SEC will transmit all significant evidence of violations of the FCPA to the Justice Department.

2. Modification of the "Reason to Know" Standard.—The FCPA currently prohibits corporate payments to agents when a company knows or has "reason to know" that all or a portion of the payment will be passed on to a foreign government official. Secretary of Commerce Baldrige testified on June 10, 1986 that this provision causes real concerns among corporate officials because "they have no idea when they might be found to have 'reason to know' about a bribe paid by an agent without their authorization." Calman Cohen, vice president of the Emergency Committee for American Trade (ECAT), also testified that "no provision of the FCPA has caused American business greater problems * * *" because "responsibility attaches under the 'reason to know' provision regardless of whether the U.S. business intends to have the third person make an improper payment." At that same June 10 hearing, Allen B. Green, representing the Public Contract Law Section of the American Bar Association, stated that:

> The effect of the uncertainty in application of the "reason to know" standard is that we of the Section cannot advise our clients that (inadvertent) conduct will be treated any less harshly than intentional bribery, which has the natural effect of discouraging international transactions.

While there was no evidence presented that the Justice Department ever abused the "reason to know" standard to prosecute inadvertent conduct, the Committee approved changes in the standard to ensure against the possibility of any future abuse. The new section 104(b) would make it unlawful for any domestic concern corruptly to "direct or authorize, expressly or by a course of conduct," a third party to bribe a foreign official. (See section 704.) The addition of the words "expressly or by a course of conduct" to the direct or authorize standard are meant to prevent management from adopting "head-in-the-sand" approach to bribery in order to avoid liability by ignoring actual facts and circumstances underlying the subject transaction which would indicate the payment of a bribe.

The Committee amendment is meant to remove ambiguities surrounding the present standard. It is not intended to change the present enforcement policy of the Department of Justice. Deputy Assistant Attorney General John Keeny of the Justice Department stated at the June 10, 1986 hearing that:

> * * * the policy of the Department has been to prosecute only those cases where the evidence of awareness—whether direct of circumstantial—was so clear as to constitute actual knowledge of the bribe scheme. This policy would not be changed by abolishing the "reason to know" standard in favor of a more objective standard and would improve the clarity of the Act.

The Committee intends that the term "course of conduct" used with the term "authorize" in section 104(b) should refer to those situations where a company, or any officer, director, employee or shareholder thereof, through its words or course of conduct, has directed or authorized that a corrupt payment be made. For example, a company's refusal or failure to respond to an agent's suggestion or request that a corrupt payment be made would violate this section, as would a company's continuing employment of an agent known to the company to have made corrupt payments in the preceding two years in violation of applicable U.S. laws or those of the country in question.

On the other hand, the mere fact of doing business in a country where corrupt payments are common, or the employment of an agent with personal relationships with government officials in the country where the company seeks to do business, would not establish such a course of conduct. Similarly, the payment of a commission that is higher than customary would not by itself violate this section without other evidence that the increased amount of commission is to permit a corrupt payment to be made.

The Committee believes that this standard will result in liability being imposed in overseas bribery cases brought under this Act if liability would also be imposed if the case were subject to domestic bribery law. The new standard is meant to continue to cover prosecution for conspiracy as well as liability for the acts of an agent within his scope of employment.

3. Facilitating and Other Payments.—The new section 104(c) which the Committee's amendments add to the FCPA is intended to eliminate the ambiguities of the current law concerning facilitating and other payments. As noted above, the present FCPA contains an exemption for such payments by excluding from the definition of the term "foreign official" an employee "whose duties are essentially ministerial or clerical." The Banking Committee report on the 1977 bill which became our current law states:

> The statute covers payments made to foreign officials for the purpose of obtaining business or influencing legislation or regulation. The statute does not, therefore cover * * * payments such as payments for expediting shipments through customs, or placing a transatlantic telephone call, securing required permits, or obtaining adequate police

protection, transactions which may involve even the proper performance of duties.

Notwithstanding the intent to exempt facilitating payments from the FCPA's bribery prohibition, the method chosen by Congress in 1977 to accomplish this has been difficult to apply in practice. Calman Cohen, the vice president of ECAT explained at the June 6, 1986 hearing the difficulties corporations encounter in determining whether a foreign official's duties are "ministerial or clerical". The Committee's amendments to this provision of the FCPA, therefore, focus the exception on the purpose of the payments rather than on the recipient. It provides that the following types of payments are permissible under the FCPA:

(1) any facilitating or expediting payment to a foreign official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official;

(2) any nominal payment, gift, offer, or promise of anything of value to a foreign official which constitutes a courtesy, a token of regard or esteem, or in return for hospitality;

(3) any reasonable and bona fide expenditures, including travel and lodging expenses, incurred by or on behalf of a foreign official, which are associated with the selling or purchasing of goods or services or with the demonstration or explanation of products; or

(4) any reasonable and bona fide expenditures, including travel and lodging expenses, incurred by or on behalf of a foreign official, which are associated with the performance of a contract with a foreign government or agency thereof.

The Committee amendments adopt another exception to the bribery prohibition in terms of an affirmative defense. That provision provides:

> It shall be an affirmative defense to any violation of this Act that a payment, gift, offer or promise of anything of value to a foreign official is lawful under the law and regulations of the foreign official's country.

The Committee amendments also define the terms "routine governmental action" and "nominal" as used in exceptions one and two above. The Committee wishes to emphasize that these four types of permissible payments and the affirmative defense should not be interpreted to undermine the basic anti-bribery purpose of that statute. The language in these exceptions and the defense is not intended to encompass corrupt payments either for the obtaining or retaining of business. Under the affirmative defense provision a company must be able to defend its actions by documenting that they are in fact "lawful" in the host country. Under the exception for nominal payments which constitute "a courtesy, a token of regard or esteem, or in return for hospitality" a particular dollar value was not placed on such payments in recognition that local customs and practices vary and appropriateness could not therefore be determined solely on the basis of U.S. dollar value. The issue to be resolved in a prosecution would be whether the value was appropriate in the context of the type of transaction being undertaken, local custom and business practices, and the laws and regulations of the host country. Similarly, the exceptions for reasonable and bona fide expenditures associated with selling or purchasing goods, or the performance of a contract with a foreign government or agency thereof must encompass only legitimate expenses made to or for the foreign official in payment for or reimbursement of that foreign official's expenses. These terms should, of course, be interpreted in a common sense manner. For purposes of the Committee amendments, "routine governmental action" means an action which is ordinarily and commonly performed by a foreign official, and includes but is not limited to payments for:

(a) obtaining permits, licenses or other governmental approvals to qualify a person to do business in a foreign country;

(b) processing governmental papers, such as visas and work orders;

(c) loading and unloading cargoes;

(d) scheduling inspections associated with contract performance; and

(e) protecting perishable products or commodities from deterioration.

The Committee emphasizes that these exceptions are not intended to encompass corrupt payments which are made either for the obtaining or retaining of business.

4. Exclusivity Provision.—The amendments also address the potential problem that conduct, which would be lawful under the FCPA, could nevertheless be prosecuted under the mail or wire fraud statutes, with prosecution based on the theory that those statutes could be used to allege that a foreign official violates a fiduciary duty to his country. The bill would preclude prosecutions, based upon that theory, except insofar as charges are brought for purposes of plea bargaining. [See section 705.]

CONCLUSION

The Banking Committee believes that enactment of the FCPA was a positive and significant step toward the important objective of prohibiting bribery of foreign government officials by United States companies in order to obtain, retain or direct business. The Congress in enacting thew FCPA did not intend to restrict or discourage legitimate export transactions. The Committee believes the amendments to the FCP in title VII will clarify ambiguities in the present statute and relieve legitimate concerns by U.S. businessmen without changing the basic intent or effectiveness of the law. In fact, it is the Committee's hope that by clarifying the law that its effectiveness and enforcement will be improved.

International business transactions which take place in cultures far different than our own sometimes involve very complex judgements. It is the U.S. business community operating abroad that must, in the first instance, judge the ethics of its actions. A clearer law will assist U.S. businessmen to police their own actions with greater confidence and will reaffirm our national policy against using bribes to obtain, retain, or direct business.

UNITED STATES TRADE ENHANCEMENT ACT OF 1987

SECTION BY SECTION SUMMARY

Title I—Export Administration Act Amendments

Section 101—Distribution License. This section would permit the granting of distribution licenses, currently unavailable for exports to controlled countries, for exports to the People's Republic of China. A distribution license permits an exporter to sell a range of goods within a particular category of technology designated by the license. This is in contrast to an individual validated license, which applies to the sale of a particular good. This is an amendment to Section 4(a)(2)(A) of the Export Administration Act of 1979, hereinafter referred to as FAA.

Section 102—General License for Reliable End-users. This section would provide for a general license for exports to end-users certified as reliable by the Secretary of Commerce. Government entities and government controlled entities from a country that maintains export controls on goods and technology pursuant to the agreement of the government with the United States to maintain export restrictions comparable in practice to those maintained by the Coordinating Committee as provided in Section 5(k) of the Export Administration Act, known as 5(k) countries, are to be considered qualified and reliable end-users. The Coordinating Committee (CoCom) is an international organization made up of the NATO countries (except for Iceland) and Japan through which the western countries enforce export controls. Amends FAA Section 4(a)(3).

Section 103—Fees. This section would prohibit the levying of a fee for the submission or processing of an export license application. Amends FAA Section 4 by adding a subsection (g).

Section 104—Exports to Members of Coordinating Committee. This section would eliminate the license requirement for exports to CoCom countries and countries which have bilateral export control agreements with the U.S. under Section 5(k) of the Export Administration Act if the exports fall below the technology level of goods which CoCom would allow to be shipped to the People's Republic of China with only a notice requirement to the participating governments of CoCom (known as the PRC greenline). This section would also give the Commerce Secretary authority to require a notice of sale of any export under this required of a particular consignee of if the Secretary determines that the country to which the export is being sent it not complying with the CoCom agreement or other applicable agreement. Amends EAA Section 5(b)(2) by adding subsections (A), (B) and (C).

Section 105—Exports to Noncontrolled Countries. This section would delicense exports, which fall below the so-called AEN (Administration Exception Notice) technology level set by CoCom, to non-Eastern Bloc countries. The AEN technology level is a level of technology for which CoCom requires only that notice of sale of an export to a controlled country be provided to CoCom's participating governments. This section also gives the Commerce Secretary discretionary authority to require that notice be provided to the Commerce Department of the sale of an export under this section. Amends EAA Section 5(b) by adding subsections (3)(A) and (B).

Section 106—Authority for Re-exports.

Subsection 106(a)—Finished Goods. This subsection would eliminate any license requirement for re-exports of finished U.S. goods to CoCom countries or countries which have bilateral export control agreements with the U.S. (5(k) countries) and require that only a notice be given to the Commerce Department. The Secretary of Commerce would retain authority to require a license for specific highly critical goods which he determines to be unilaterally controllable. Amends EAA Section 5(b) by adding subsection (4).

Subsection 106(b)—Components. This subsection would eliminate any license requirements for the re-export of any U.S. good or technology from any foreign country if the good or technology is incorporated into other products for which no license is required and the value of the U.S. content of the product is 20% or less. The Commerce Secretary would retain authority to require a license for the re-export of incorporated goods or technology if the Secretary determines them to be highly critical. Amends EAA Section 5(b) by adding subsection (5).

Section 107—Control List Disputes. Current law provides that when the Secretary of Commerce and the Secretary of Defense are unable to agree on whether an item should or should not be on the control list, the matter should be referred to the President for resolution. This section provides that the President should resolve such disputes in a timely manner consistent with the dispute settlement procedures set forth in section 10(g) of the EAA. Amends EAA Section 5(c)(2).

Section 108—CoCom Review Process. This section clarifies that it is the responsibility of the Secretary of Commerce to formulate United States positions for CoCom negotiations on list review, license applications, and determining whether export restrictions maintained by other countries are comparable in practice to those in CoCom. The Secretary of State is responsible for actually negotiating in CoCom meetings. Amends EAA Section 5(c)(3).

Section 109—Elimination of Unilateral Controls. This section would have the Secretary of Commerce review on a yearly basis all items on the control list maintained unilaterally by the United States and eliminate from that list all items except those goods or technologies for which there is no foreign availability or on which multilateral negotiations are underway. The Secretary must submit for publication in the Federal Register each year a list of those items still unilaterally controlled with a specific justification for control of each item. Amends EAA Section 5(c) by adding subsection (4).

Section 110—Sunset Provision. This section would specify that if an item on the control list has not been reviewed for two years, even though the law requires annual review of the list, and if the item is below the PRC greenline and an exporter seeks a review, the Secretary has 90 days to complete a review of that item and submit the findings for publication. If the review and submission for publication are not completed within 90 days, the item is then automatically removed from the control list. Amends EAA Section 5(c) by adding subsection (5).

Section 111—Trade Shows. This section states that there shall be a presumption of approval to license any goods or technologies on the commodity control list for the purpose of exhibition or demonstration at a U.S.-sponsored trade show for the exports to the People's Republic of China so long as the U.S. exporter retains title to the goods and the goods are U.S. marketing efforts in the PRC. Amends EAA Section 5(e) by adding subsection (6).

Section 112—Foreign Availability Determinations.

Subsection 112(a)—Procedures. The Export Administration Act requires the Commerce Secretary to delicense the export of a good if Secretary determines that the good is already available to a controlled country in sufficient quantity and of comparable quality so that requirement of a validated license for the export of the good would be ineffective. This subsection would require the Commerce Secretary to determine within 60 days whether foreign availability of a good or technology exists. If a final determination is not possible within 60 days, the Secretary would have an additional 60 days to make a final determination. If no determination is made within 120 days, the Secretary may not require a license for the export of the good. This amendment does not affect the provisions of existing law (Section 5(f)(1)) which permits the President to control items, despite a finding of foreign availability, if to decontrol the item would prove detrimental to the national security. In any such case the President has a maximum period of 18 months to negotiate away foreign availability of the item. Amends EAA Section 5(f) and 5(f)(3).

Subsection 112(b)—Authority of Secretary. This provision amends existing law to make clear that the Secretary of Commerce can make foreign availability determinations without the concurrence of other departments or agencies. Amends EAA Section 5(f)(1).

Subsection 112(c)—Publication of Availability Assessments. This subsection requires the Commerce Secretary to publish notice of a foreign availability assessment in the Federal Register. Amends EAA Section 5(f) by adding subsection (8).

Section 113—Foreign Availability. This section would amend the current law to specify that the President shall notify the appropriate Congressional committees when negotiations to eliminate the foreign availability of such items begins and to explain why national security controls are being maintained despite foreign availability. Amends EAA Section 5(A)(4).

Section 114—Review of Technology Level. This section requires the Secretary of Commerce to annually review the performance level of goods or technology of the PRC greenline, CoCom, and 5(k) country agreement groups and to make appropriate decontrol adjustments based on those reviews. Amends EAA Section 5(g).

Section 115—Negotiations to Improve Multilateral Cooperation. This section directs the President to enter into negotiations with the member governments of CoCom to improve cooperation within CoCom to obtain agreements with non-CoCom governments to restrict the export of goods and technology on the International Control List. Amends EAA Section 5(i).

Section 116—Export Controls on Goods Containing Controlled Parts and Components. This section amends the current law to broaden the definition of goods containing microprocessors. Current law decontrols goods containing "embedded" microprocessors when the overall function of the good does not merit control. Technological advances have caused a shift from the use of proprietary embedded microprocessors to operate products to the use of commercial microprocessors and personal computers to "drive" systems, often as peripheral, plug-in components. This change broadens the language of current law to accommodate these advances within the constraint that the components be no more than 20% of total value. Controls would be maintained over complete systems that would contribute to the military potential of a controlled country. Amends EAA Section 5(m).

Section 117—Foreign Availability to Other Than Controlled Countries. The Export Administration Act requires the Commerce Secretary to delicense the export of a good if the Secretary determines the good is already available to a controlled country in sufficient quantity and of comparable quality so as to make continue export controls on the item ineffective in achieving the goal of denying such item to a controlled country. Section 5(f) of existing law, as amended by Section 112 of this Title, sets forth the procedures for making foreign availability determinations with regard to exports to controlled countries. This section establishes procedures for making foreign availability determinations to non-controlled countries. It provides that if the Secretary determines that an item is available in sufficient quantity and comparable quality in a country, other than by export under license from a CoCom or Section 5(k) country, the Secretary should delicense that product to all free world destinations to which the country in question ships without controls. The presumption behind this provision is that U.S. producers should not be denied markets in which goods from competing countries are freely available. It is also based on the premise that an item would in fact be available to a controlled country if it is available in a non-controlled country that is not cooperating in export control efforts. The section establishes time frames for the Secretary to make foreign availability determinations and also provides that the Secretary may still control exports of items if the President determines that it is important to the national security to do so. In the latter case, the President would have 6 months to negotiate away foreign availability (with up to a 12 month extension) and if the negotiation was unsuccessful, the item would have to be decontrolled.

Section 118—Sharing of Information on Foreign Availability. This section provides that in order to assist the Department of Commerce to make foreign availability determinations each department or agency of the United States, including intelligence agencies, and contractors with such departments and agencies, shall at the request of the Secretary and consistent with protecting intelligence sources and methods, furnish requested information to the Secretary of Commerce Office of Foreign Availability. Amends EAA Section 5 by adding subsection (s).

Section 119—Foreign Policy Controls. The Export Administration Act gives the President authority to impose export controls to further the foreign policy objectives of the United States. This section directs the President to employ diplomatic alternatives before imposing foreign policy export controls. It also provides that foreign policy controls will not cover shipments of spare parts on previously sold items that is specifically provided in the controls by the President. Amends EAA Section 6(a).

Section 120—Refined Petroleum Products. This section states that no export controls or restrictions shall be applied to refined petroleum products of refineries within the United States unless the President determines that controls or restrictions are necessary. This section reaffirms existing law, as stated in EAA Section 7(e). Amends EAA Section 7 by adding a new subsection (k).

Section 121—National Security Review. Section 10(g) of the Export Administration Act gives the Secretary of Defense authority to review national security export license applications to countries to which exports are controlled for national security purposes. This section would amend section 10(g) of the law to require the Defense Secretary to make a recommendations within 20 days of receiving an application. If no recommendation is made within 20 days, the Commerce Secretary would have authority to approve or deny a license. This section also strikes out Section 10(g)(4) of the Export Administration Act, which requires the President to notify Congress if the President overrules a recommendation made by the Defense Secretary. Amends EAA Section 10(g).

Section 122—Sanctions for Export Violations. This section would amend section 11(c) of the law to state that access to U.S. Government procurement may be denied for a period of up to five years to any foreign person who violates national security controls issued pursuant to a CoCom agreement. Amends EAA Section 11(c).

Section 123—Prior Convictions. Section 11(L) of the Export Administration Act provides that no person convicted of a violation of various crimes shall be eligible, at the discretion of the Secretary, to apply for or use any export license under the EAA for a period of up to 10 years from the date of conviction. This section makes technical changes in referencing the specified crimes in the statute. It also provides that the Secretary's authority to deny exports can apply to corporations or business organizations under the control of the convicted person. Amends EAA Section 11(h).

Section 124—Judicial Review. The Export Administration Act is exempted from the Administrative Procedures Act which would give parties regulated by the EAA the right of judicial review. This section gives parties the right of judicial review under the Export Administration Act when a civil penalty or other sanction is imposed for violation of the Act or when a temporary denial order is granted under the Act. Other provisions of the EAA remain exempt from this limited judicial review provision. Amends EAA Section 13(c).

Section 125—Issuance of Temporary Denial Orders. Section 13(d) of the EAA gives the Secretary of Commerce the right to issue a temporary order denying a person a right to export if it is necessary to prevent an imminent violation of the Act. These technical changes to that provision would also permit the Secretary to temporarily deny exports for the purpose of facilitating enforcement of the Act. Amends EAA Section 13(d).

Section 126—Responsibilities of the Undersecretary of Commerce for Export Administration. This section adds responsibility for export administration national security issues to the position of the Undersecretary of Commerce for Export Administration. Under this provision, administration of short supply controls and agency responsibilities for national security programs including the Defense Production Act of 1950 would fall to the Undersecretary. Amends EAA Section 15(a).

Section 127—Authorization of Appropriations. This section authorizes appropriations for the functions of the Office of the Undersecretary of Commerce for Export Administration of $45,248,000 for each of the fiscal years 1988 and 1989. Of this amount, $40,248,000 represents the level of funding requested by the Administration for Export Administration activities and for administration of short supply controls and national security program responsibilities which would fall under the new Undersecretary as provided in Section 126 above. The remaining $5,000,000 is intended to cover the start-up and ongoing administrative costs of the new Office of the Undersecretary, and is offset by a reduction of funds authorized for other programs of the International Trade Administration. This section also provides that no transfer of funds from appropriations for this new Office can be made in payment of shared administrative expenses or support without the concurrent of the Undersecretary of Commerce for Export Administration. Amends GAA Section 18(b) by adding subsection (4).

Section 128—General Accounting Office Report. This section directs the GAO to review the effect of the amendments made by this Act and report back to the Congress by March 1, 1989.

Title II—Export Trading Companies

Section 201. Determination of Classification as Export Trading Company. Under the Export Trading Act a bank-affiliated ETC must be operated "principally for the purpose of exporting", and the Federal Reserve has established a revenue test requiring that an ETC derive more than 50% of its total revenue from exporting. Currently income earned from promoting exports between third countries does not count as revenue from exporting. This provision would allow export trading companies (ETCs) to count fees derived from facilitating exports between third countries as revenue derived from exporting so long as the fees are remitted to the U.S. and the aggregate amount of the fees in any one year does not exceed one-fifth the amount of revenues actually derived from promoting U.S. exports.

Section 202. Leverage. Federal Reserve regulations require that any ETC with a proposed assets-to-equity ratio of more than 10–1 must have its notice reviewed in Washington rather than at a regional Federal Reserve Bank. This provision states that the Federal Reserve Bank may not disapprove an application solely on the basis of a proposed asset-to-equity ratio unless the anticipated or proposed annual average asset-to-equity ratio is greater than 15–1.

Section 203. Inventory. Federal Reserve regulations require that the application for an ETC that plans to hold more than $2 million of goods in inventory be reviewed in Washington in order to prevent risks to any investor bank holding company. This provision would eliminate the $2 million limit but give the Fed authority to set a dollar limitation on the value of goods which any individual ETC may keep in inventory at any time on a case-by-case basis.

Section 204. Office of Export Trade. This provision amends the ETC Act by directing the referenced office in the Commerce Department to establish a program to encourage and assist other export intermediaries including export management companies.

Section 205. Report on Export Promotion Intermediaries. This provision requires the Secretary of Commerce to provide a comprehensive report to Congress within 18 months of the enactment of this section describing the Department's activities with respect to promoting and encouraging the formation and operation of the full range of export promotion intermediaries, including export management companies, export trade associations and export trading companies.

Title III—Export Promotion

Section 301. Export Promotion Activities of Foreign Commercial Service Officers. This provision would require the Secretaries of State and Commerce to review periodically the number of foreign commercial service officers in U.S. diplomatic missions to determine if there are a sufficient number. It would also require the chief of each U.S. diplomatic mission to a country which is an important U.S. trading partner to submit yearly reports to the President and Congress on its efforts to expand U.S. exports. It also declares the sense of the Congress that each U.S. executive director to a multilateral development bank should assist U.S. firms in bidding for procurement opportunities in recipient countries, and a foreign commercial service officer should be assigned to each U.S. executive director for that purpose.

Section 302. Collection and Dissemination of Trade Information. This provision directs the Secretary of Commerce, acting through the International Trade Administration and with available resources, to gather information on a country by country basis collected by federal agencies which would be useful to firms engaged in exports and to set up an information system to disseminate the data to private sector businesses and State export agencies for a fee. The Secretary shall report to Congress within 6 months of the enactment of this bill the status of the implementation of said system.

Section 303. Multilateral Development Bank Liaison. This provision directs the Secretary of Commerce to designate an office of the International Trade Administration to act as business liaison with multilateral development banks which do not have offices in the U.S.

Section 304. Rank of Commercial Officers. This provision authorizes the Secretary of Commerce to designate 8 U.S. missions abroad at which the senior U.S. and Foreign Commercial Service officer would be able to use the diplomatic title of Minister-Counselor.

Section 305. Catalog of U.S. Government Resources. This provision directs the Secretary of Commerce to prepare within one year a reference manual for U.S. business firms listing all sources of information within the U.S. Government related to exporting, foreign investment, foreign market conditions, foreign laws and regulations affecting exports, and sources of export and foreign investment finance.

Title IV—Exchange Rates and International Economic Policy Coordination

Section 401—Short Title. This section states that the title may be cited as the Exchange Rates and Economic Policy Act of 1987."

Section 402—Findings and Purposes.

Section 402(a)—Findings. This section finds that the macroeconomic policies of the leading industrialized nations lack coordination and that currency values as a result are not aligned in a manner consistent with long-term economic growth; a pattern of exchange rates has developed which produces persisting imbalances between nations; policy initiatives by some major trading nations to manipulate the rate of exchange between their currency and the U.S. dollar create serious competitive problems for U.S. industries; a more stable exchange rate for the dollar at a level which will permit a substantial reduction in the U.S. trade deficit should be a major focus of national economic policy; under appropriate circumstances, intervention by the U.S. in foreign exchange markets as part of a coordinated international intervention could produce more orderly adjustment of foreign exchange markets.

Section 402(b)—Purposes. This subsection states that it is the purpose of this title to encourage the President to negotiate with other countries to achieve better coordination of macroeconomic policies, greater stability in trade and current account balances, greater coordination of the participation of central banks in international currency markets, and increased accountability for the impact of exchange rates on trade competitiveness.

Section 403—Definitions. This section defines terms for purposes of the Act.

Section 404—International Negotiations on Exchange Rates and Economic Policy Coordination.

Subsection 404(a)—Statement of Policy. This subsection states that it is the policy of the United States that the U.S. and other major industrial countries should take steps to institutionalize the process of coordinating monetary and fiscal policies begun at the Tokyo Economic Summit in May 1986. The goal of policy coordination should be to eliminate imbalances in trade and capital flows and to stabilize exchange rates. The U.S. and other major industrial countries should also coordinate central bank intervention in the currency markets where appropriate to stabilize exchange rates.

Subsection 404(b)—International Negotiations on Exchange Rates. This subsection directs the President to negotiate with other countries to achieve better coordination of macroeconomic policies of the major industrialized countries, to review the functioning of the exchange rate system, and to develop a program to modify the system to provide for long-term exchange rate stability.

Subsection 404(c)—Bilateral Negotiations. This subsection directs the President to initiate negotiations with countries which manipulate the rate of exchange between their currency for commercial advantage and have both material global account surpluses and significant bilateral trade surpluses with the U.S. to ensure that such countries regularly and promptly adjust the rate of exchange between their currency and the U.S. dollar.

Section 405—Reporting Requirements.

Subsection 405(a)—Reports Required. This subsection directs the Secretary of the Treasury to submit annual written reports and to testify annually on international economic policy to the House and Senate Banking Committees.

Subsection 405(b)—Contents of Report. This subsection requires that the report contain the results of negotiations conducted under subsections 404(a) and (b), an assessment of the impact of the exchange rate of the dollar on the ability of the U.S. to maintain a sustainable balance in its current account, a statement of proposed changes in U.S. economic policy likely to impact the current account position, an analysis of the exchange rate trends and economic policies of any countries with which the U.S. has substantial bilateral trade or capital flows, and a report on the impact of capital flows on exchange rates and trade.

Subsection 405(c)—Report by Board of Governors. This subsection amends the Federal Reserve Act to require the Federal Reserve Board to include in its annual report to Congress an analysis of the impact of the dollar's exchange rate on national economic trends.

Title V—International Debt

Subtitle A—General Provisions

Section 501—Findings. This section finds that the international debt problem threatens the safety and soundness of the international financial system, the stability of the international trading system, and the economic development of the debtor countries. Growth in the debtor countries has been constrained by their debt service obligations and insufficient new financial resources, forcing them to reduce imports and expand exports. The U.S. has borne a disproportionate share of the burden of absorbing exports from debtor countries. Current approaches to the debt problem should not rely solely on new lending as a solution, and should focus on other financing alternatives including a reduction in current debt service obligations. New international mechanisms to improve the management of the debt problem and to expand the range of financing options for the debtor countries should be explored.

Section 502—Purposes. This section states that the purposes of this title are to expand the world trading system and raise the level of exports from the U.S. to the developing countries, alleviate the international debt problem to permit growth in the debtor countries, and to increase the stability of the world financial system and insure the safety and soundness of U.S. depository institutions.

Section 503—Statement of Policy. This section states that it is the policy of the U.S. that increasing developing world growth is a major goal of international economic policy, it is necessary to broaden the range of options in dealing with the debt problem to include improved mechanisms to restructure existing debt, active consideration of a new multilateral intermediary to improve the management of the debt problem must be undertaken, and countries with strong current account surpluses bear a major responsibility for providing the financial resources needed for growth in the developing world.

Subtitle B—The International Debt Management Authority

Section 511—Short Title. This section states that this subtitle may be cited as the "International Debt Management Act."

Section 512. International Discussions.

Subsection 512(a)—Directive for Discussions. This subsection directs the Secretary of the Treasury to initiate discussions with industrialized and developing countries to propose the establishment of a multilateral financial intermediary which would be authorized to purchase sovereign debt of less developed countries from private creditors at an appropriate discount, enter into negotiations with the debtor countries to restructure the debt, and assist creditor banks in the voluntary disposition of their Third World loan portfolio.

Subsection 512(b)—Objectives. This subsection states that in the discussions the Secretary should propose that support for the authority come from industrialized countries, particularly from countries with strong current account surpluses; the authority should have a close working relationship with the IMF and the World Bank; the authority should be a self-supporting entity, requiring no routine appropriation from any member government; and that the authority should have a defined termination date.

Subsection 512(c)—Interim Reports. This subsection directs the Secretary to submit reports to the House Banking Committee and the Senate Banking and Foreign Relations Committees on the progress in the discussions six months and eighteen months after the enactment of this Act.

Subsection 512(d)—Final Report. This subsection directs the Secretary to submit reports to the House Banking Committee and the Senate Banking and Foreign Relations Committees upon the conclusion of the discussions.

Section 513—Actions to Facilitate Creation of the Facility. This section directs the Treasury Secretary to review all potential resources available to the U.S. and the multilateral financial institutions to support the creation of an international debt management facility, including a determination of the gold stock of the IMF that could be pledged as collateral to obtain financing for the facility.

Section 514—Reducing Capital Flight. This section states it is the sense of the Congress that a solution to the practice of capital transfers from developing countries is essential to solving the international debt problem, and the U.S. Executive Director to the IMF should initiate discussions with other directors of the Fund to develop proposals to reduce the level of capital transfers and report any such proposal to the Treasury Secretary and the Chairman of the Federal Reserve.

Subtitle C—Regulatory Provisions Affecting International Debt

Section 521—Statement of Policy. This section states that it is the policy of the U.S. that commercial banks should establish sufficient reserves against the risks inherent in international lending and, within regulatory constraints, should have significant latitude to restructure the terms and conditions on their existing international loans so that additional new lending is not the only option available.

Section 522—Facilitation of Debt for Equity Exchanges.

Subsection 522(a). This subsection directs the Federal banking agencies to conduct a study of any regulatory or accounting barriers to exchanges of foreign debt for equity and to report back to Congress by Jan. 15, 1988.

Subsection 522(b). This Subsection directs the Secretary of the Treasury to instruct the U.S. Executive Director of the World Bank to initiate discussions with other directors of the Bank on the appropriate role for the World Bank and the International Finance Corporation in supporting debt-to-equity swaps.

Section 523—Regulatory Study. This section directs the Secretary of the Treasury, along with appropriate Federal banking agencies, to submit a report to Congress within six months of the enactment of this Act analyzing possible regulatory steps to encourage a reduction in the indebtedness of heavily indebted international borrowers to supervised banks in a way that would improve overall bank asset quality and reduce the burden of the debt on the countries themselves.

Title VI—National Treatment of Financial Institutions

Section 601—Effectuating the Principle of National Treatment for Banks. This section permits the Federal banking agencies, with the prior approval of the President, to deny applications and disapprove notices filed by banks and bank holding companies from countries that do not accord national treatment to U.S. banks and bank holding companies. The authority is purely discretionary; the bank agencies and the President are not required to act. The requirement of prior Presidential approval is intended to ensure that any exercise of that authority be consistent with overall foreign policy.

The definition of national treatment in this section (that the country in question "accord[s] to United States banks and bank holding companies the same competitive opportunities as it accords to domestic banks and bank holding companies") is drawn from, and intended to have the same meaning as, the definition in the Treasury Department's National Treatment Study.

This section applies to any application by a foreign bank or bank holding company that requires the approval of a Federal banking agency, including an application to acquire shares of a bank or bank holding company, to engage in nonbanking activity, to establish a Federal branch or agency, or to obtain Federal deposit insurance. It applies equally to any notice by a foreign bank or bank holding company that is subject to disapproval by a Federal banking agency, such as a notice under the Change in Bank Control Act.

Section 602—Requirement of National Treatment in Underwriting Government Debt Instruments. This section seeks to encourage foreign countries to end discrimination against U.S. companies in the underwriting and distribution of government debt instruments.

Subsection (a)—Findings. This subsection makes findings relating to the discrimination of Japanese Government debt instruments. Although this section is prompted by concerns about discrimination in Japan, it applies to companies owned or controlled by any person of a foreign country, except as otherwise provided in subsections (b) and (c).

Subsection (b)—Designation of Certain Persons as Primary Dealers Prohibited. Effective two years after this bill becomes law, this subsection prohibits the Federal Reserve System from designating any person of a foreign country as a primary dealer, or continuing any prior designation of such a person as a primary dealer, unless the foreign country in question accords U.S. companies national treatment in the underwriting and distribution of government debt instruments issued by that country. The definition of national treatment in this subsection (that the country in question "accord[s] to United States companies the same competitive opportunities . . . as it accords to domestic companies"), like the definition in section 601, is drawn from and intended to have the same meaning as the definition in the Treasury Department's National Treatment Study.

This subsection does not apply to any previously designated primary dealer of which ownership or control was acquired by a person of a foreign country before January 1, 1987. To come within that grandfather provision, the company must have been designated as a primary dealer before the person of a foreign country acquired ownership or control of it, and that ownership or control must have been acquired before January 1, 1987, Thus if a person of a foreign country acquired ownership or control of a company before the company was designated a a primary dealer, the grandfather provision does not apply to that company.

Apart from the specific prohibitions of this subsection, this section does not impair the Federal Reserve's current discretion to designate or refuse to designate anyone as a primary dealer, or to continue or rescind anyone's designation as a primary dealer. Accordingly, the Federal Reserve retains the same discretion as it has under existing law to rescind a company's designation as a primary dealer, even if the company is grandfathered under this subsection or excepted under subsection (c).

"Company", as used in this section, encompasses any business entity.

Government debt instruments are "issued by [a foreign] country" for purposes of this subsection if they are issued by the national government of that country.

Primary dealers are currently designated by the Federal Reserve Bank of New York. See BankAmerica Corporation, 73 Fed. Reserve Bull. 361, 362 n.2 (1987). But because the prohibitions of this subsection extend to the Federal Reserve Board, they would apply even if primary dealers were designated by the Board or by some other unit of the Federal Reserve System.

Subsection (c)—Exception for Countries Having or Negotiating Bilateral Agreements with the U.S. This subsection excepts a person of a foreign country from the prohibitions of subsection (b) if the foreign country in question either (1) was negotiating a bilateral agreement with the United States, as of January 1, 1987, pursuant to section 102(b)(4)(A) of the Trade Act of 1974 (19 U.S.C. 2112(b)(4)(A)); or (2) has a bilateral free trade area agreement with the United States which entered into force before January 1, 1987.

As of January 1, 1987, the United States was negotiating a bilateral agreement with Canada pursuant to section 102(b)(4)(A) of the Trade Act of 1974. A bilateral free trade area agreement between the United States and Israel entered into force in 1985. Accordingly, subsection (b) does not apply to a company because of that company being under Canadian or Israeli ownership or control.

Subsection (d)—"Person of a Foreign Country" Defined. Under this subsection, a person is a "person of a [given] foreign country" if that person, or any person that directly or indirectly controls that person, is a resident of that country, is organized under the laws of that country, or has its principal place of business in that country. A company can thus be a person of more than one foreign country.

Subsection (e)—Effective Date. The objective of this section is to encourage foreign countries to end discrimination against U.S. companies in the underwriting and distribution of government debt instruments, rather than to exclude foreign companies from the United States. Accordingly, subsection (e) delays the effective date of this section for two years in order to give foreign countries ample time to come into full compliance with the standard of national treatment.

Title VII—Foreign Corrupt Practices Act Amendments

Section 701—Short Title. This Section simply provides that this Title may be cited as the Foreign Corrupt Practices Act Amendments of 1987.

Section 702—Findings and Conclusions.

(a) Findings. This Section contains three Congressional findings noting the significant contribution Congress made in enacting the Foreign Corrupt Practices Act (FCPA) in 1977 but also citing the unnecessary concerns the Act has raised among legitimate exporters and the unnecessary and costly paperwork burdens it has imposed on all issuers of securities.

(b) Conclusions. This Section states that Congress concludes that the principal objectives of the FCPA should be maintained because they are important to the nation and that exporters should not be subject to conflicting demands from the diverse agencies enforcing the FCPA.

Section 703—Penalties for Violations of Accounting Standards. This Section provides that no criminal liability shall be imposed for failing to comply with the FCPA's books and records or accounting control provisions unless a person knowingly circumvents a system of internal accounting controls or knowingly falsifies books, records, or accounts kept pursuant to Section 13(b)(2) of the Securities Exchange Act of 1934. In addition the Section adds a new paragraph (b)(6) to that provision of the Securities Act which defines the responsibility of an issuer with respect to the accounting practices of a domestic or foreign subsidiary in which the issuer owns an interest of 50 percent or less. It also provides that for purposes of Section 13(b)(2) the term "reasonable assurances" and "reasonable detail" mean such level of detail and degree of assurance as would satisfy prudent officials having in mind a comparison between benefits to be obtained and costs to be incurred in obtaining such benefits.

Section 704—Repealer: New Bribery Provisions.

(a) Repeals. This Section would place in the Justice Department all jurisdiction for enforcing the anti-bribery provisions of the Act. The SEC would remain responsible for civil enforcement of the books and records and internal accounting control provisions.

(b) Report. This Section provides that the SEC report evidence that an issuer is violating the Act's anti-bribery provision to the Justice Department. This provision is discretionary so that the SEC will not feel obligated to report every scintilla of bribery evidence it discovers, but is intended to ensure that the Commission well report evidence it believes warrants further discussion. The Justice Department is obligated to report to the appropriate Congressional oversight Committee's annually on such referrals from the SEC.

(c) Foreign Payments. This Section would re-write Section 104 of the FCPA. Subsection (a), designed inter alia to bring the Act into conformity with domestic bribery statutes, would prohibit a domestic concern from making use of the mails or any other instrumentality of interstate commerce to make payments for the purposes of influencing any act or decision of a foreign official in his official capacity, or inducing him to do or omit to do any act in violation of his legal duty as a foreign official, or inducing him to so use his influence, for the purposes of assisting the domestic concern in obtaining or retaining business, or of directing business to any person.

1. Agents—Subsection (b) of the section 104 rewrite would prohibit bribery through use of intermediaries. It replaces the "reason to know" standard of current law. In its place it makes it illegal for a domestic concern "corruptly to direct or authorize, expressly or by a course of conduct", bribery by means of a third party.

2. Facilitating Payments—Subsection (c) of the section 104 rewrite would exempt certain specified facilitating payments from the anti-bribery provisions. Such payments include those made to expedite or secure the performance of a routine governmental action by a foreign official and nominal payments or gifts to a foreign official which are a courtesy or token of regard or esteem. Also payments to cover reasonable and bona fide expenditures, including travel and lodging expenses, which are associated with demonstrating products or performing contracts are also exempted. None of these exceptions are intended to encompass corrupt payments either for the obtaining or retaining of business.

3. Payments Legal in the Foreign Country—Subsection (d) of the Section 104 rewrite provides that it shall be an affirmative defense to any violation of the FCPA if the payor can demonstrate that the payment, gift, offer, or promise of anything of value to a foreign official is lawful under the laws and regulations of that foreign official's country. The Committee does not intend this defense to apply to corrupt payments made either for the obtaining or retaining of business.

4. Penalties—Subsection (e) of the section 104 rewrite would continue the civil and criminal penalties provided for in current law: \$1,000,000 maximum fine for domestic concerns; for individuals a maximum fine of \$10,000 and/or up to five years imprisonment. This subsection also provides that the term "found to have violated" as used in the subsection includes a conviction based on related inchoate offenses, such as a conspiracy to violate the provisions of the Act, or on a plea of nolo contendre. This definition was included so that the Government can prosecute an individual employee of a company even when his company was convicted of only a conspiracy to violate the FCPA or pleaded nolo contendre to such a charge. Fines imposed on individuals under this subsection are not to be paid by the corporation.

5. Authority for Civil Injunction and Investigation—Subsection (f) of the section 104 rewrite would consolidate authority to obtain injunctive relief for violation of the Act in the Department of Justice, whereas current law divides the authority between the Justice Department and the SEC. The subsection adds a provision, not found in current law, authorizing the Justice Department to conduct civil investigations, and provides subpoena authority for such investigations, and provides to the Attorney General rulemaking authority to implement the civil investigation provision.

6. "Domestic Concern" and "Foreign Official"—Subsection (g)(1) of the section 104 rewrite would define "domestic concern" so as to include citizens, nationals, and residents of the U.S., and companies, business entities, or sole proprietorship which has a class of securities registered to Section 12 of the Securities Exchange Act of 1934, or which is required to file reports under Section 15(d) of the Securities Act of 1934.

Subsection 8(2) of the Section 104 rewrite defines "foreign official" so as to include officers and employees of foreign governments and agencies, political parties, party officials, and candidates.

7. "Routine Governmental Action" and "Nominal"—Subsection (g)(3) of the section 104 rewrite would make clear that the exception for payments made to secure the performance of a "routine governmental action" by a foreign official would not include payments made to influence such an official to award new business or to continue business with a particular party. Subsection (g)(4) defines the term "nominal" used to limit the size of payments or gifts that can be given to foreign officials as marks of esteem or in return for hospitality.

Section 705—Exclusivity Provision for Overseas Bribery. This Section provides that except in plea bargain situations no criminal prosecution may be brought against any person or firm alleging that the mail or wire fraud laws have been violated as a result of a foreign corrupt payment, where the prosecution is based upon the theory that the foreign official violated a fiduciary duty. Similarly no prosecution for conspiracy to violate the mail or wire fraud statute based on that theory would be permissible.

Regulatory Impact Statement

Pursuant to Rule XXVI, paragraph 11(b) of the Standing Rules of the Senate, the Committee has evaluated the regulatory impact of the bill and concludes it would result in no net increase in the regulatory burden imposed by the Government. In fact the provisions of Title I, amending the Export Administration Act, will streamline the export control process and thereby reduce the regulatory burdens on exporters. The provisions of Title VII, which amend the Foreign Corrupt Practices Act, may reduce unnecessary and costly paperwork burdens on businesses by specifically providing that management can use a cost-benefit analysis and a prudent official approach in determining the level of detail and the degree of assurance of accuracy that are needed to comply with the FCPA's books and records and accounting systems requirements.

CHANGES IN EXISTING LAW

The Committee has determined that it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of Rule XXVI, paragraph 12, of the Standing Rules of the Senate, with respect to this legislation.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, June 12, 1987.

Hon. WILLIAM PROXMIRE,
Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the attached cost estimate for the United States Trade Enhancement Act of 1987.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes,
Sincerely,

JAMES BLUM
(For Edward M. Gramlich, Acting Director).

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

1. Bill number: Not yet assigned.
2. Bill title: United States Trade Enhancement Act of 1987.
3. Bill status: As ordered reported by the Senate Committee on Banking, Housing and Urban Affairs, May 19, 1987.
4. Bill purpose: The bill authorizes $45.2 million for each of fiscal years 1988 and 1989 to carry out the functions of the Undersecretary of Commerce for Export Administration. For fiscal year 1988, $40.2 million of this amount represents funds already authorized to the Department of Commerce for export administration, short-supply controls, and administration of its responsibilities under the Defense Production Act of 1950. The bill also reduces other funds authorized for the International Trade Administration (ITA) by $5 million in each of fiscal years 1988 and 1989.

The bill contains a number of other provisions affecting the Department of Commerce that would have a cost impact if the bill were implemented. These include a requirement that the ITA publish a catalog of U.S. government sources of information for exporters, that the Secretary of Commerce designate an office of the ITA to act as a business liaison with the three multilateral development banks that do not have their main offices in the United States, and that the Office of Export Trade establish a program to encourage and assist the operation of export intermediaries other than export trading companies.

The bill also amends the Foreign Corrupt Practices Act of 1977 by revising its compliance and enforcement procedures, including transferring from the Securities and Exchange Commission (SEC) to the Department of Justice (DOJ) responsibility for enforcing certain bribery provisions of the act. In addition, the bill would require the Secretary of Treasury and other federal agencies to prepare a total of 10 reports on trade issues.

5. Estimated cost to the Federal Government: The following table shows the estimated budget impact of the specific authorizations in this bill.

[By fiscal year, in millions of dollars]

	1988	1989	1990	1991	1992
Authorization level		40.2			
Estimated outlays		28.4	7.9	3.9	

The bill also mandates certain activities on the part of the Department of Commerce and the Justice Department, but does not specifically authorize appropriations for such purposes. These activities are estimated to cost about $5 million in 1988 and approximately $2 million per year thereafter.

The costs of this bill fall within budget functions 150, 370, 750, and 800.

Basis of Estimate

This estimate assumes that this bill will be enacted prior to the beginning of fiscal year, 1988, and that the amounts authorized will be appropriated. Outlays for the Office of Export Administration are estimated based on historical spending patterns for the ongoing activities of the ITA. Costs for the other provisions affecting the Department of Commerce are estimated to be approximately $1 million annually, based on information provided by that department. To prepare the 10 studies required in the bill, it is estimated that costs of about $3 million in 1988 and $500,000 in each fiscal year thereafter would be incurred, assuming appropriations are made available for these purposes. CBO estimates that to accomplish the transfer of responsibility from the SEC to the DOJ, as required by the bill, would cost about $500,000 annually.

6. Estimated cost to State and local governments: None.

7. Estimate comparison: None.

8. Previous CBO estimate: None.

9. Estimate prepared by: Carol Cohen, Mary Maginniss, and Michael Sieverts.

10. Estimate approved by: E.G. Nuckols (for James L. Blum, Assistant Director for Budget Analysis).

ADDITIONAL VIEWS OF SENATOR PROXMIRE: TITLE V INTERNATIONAL DEBT

My additional views on this Title do not concern what is in the Title, but rather focus on a provision that was deleted from the Title at our Committee's May 19 markup. That provision would have simply required our banks, that are heavily exposed to troubled international loans, to establish a special reserve against them to buttress their own safety and soundness. The provision stated that the reserve should be in the amount of not less than 10 percent but not more than 30 percent of the institution's total exposure to international loans which the bank regulators categorize as troubled, i.e., included within the regulatory categories of "Other Transfer Risk Problems (OTRP)" of "Substandard". Banks, under the provision, would not have been able to just decrease portions of their other primary capital of build the reserves. Furthermore, the reserves could have been built over a five-year period so it would not have had a drastic impact on bank earnings. I am convinced that my colleagues on the Banking Committee made a mistake in deleting that provision which was designed to bolster the safety and soundness of our banking system. Let me explain.

During the 1970's and early 1980's, U.S. banks sharply increased their foreign lending, much of it directed toward borrowers in developing countries. By 1982 the nine largest U.S. banks, which make more than sixty percent of all U.S. banks loans to the developing countries, had more than 340 percent of their bank capital exposed in such loans. Their exposures to Argentina, Brazil, and Mexico alone accounted for almost 140 percent of their total capital.

There are, of course, legal limits as to how much a bank can loan to any one borrower. Section 80 of Title 12 of the United States Code imposes on national banks a general lending limit of 15 percent of each bank's capital funds to any one borrower. But in April 1979 the Officer of the Comptroller of the Currency (OCC) issued an interpretive ruling that in effect exempted loans to foreign countries from this provision of law. As a result of this decision by the OCC some of our large money center banks got into a position where a decision by any one country not to pay its loans threatened the stability of such banks. The remain in that position today. Citicorp has $4.6 billion in loans to Brazil, which represent 34 percent of its primary capital. Manufacturers Hanover has more than 130 percent of its primary capital exposed in loans to just five Latin debtor countries. Other large money center banks have similar exposures in these countries.

The risks to bank safety created by this situation became starkly visible in August 1982 when Mexico announced that is was unable to service its debts and shortly thereafter several other large debtor nations, including Brazil, Argentina and Venezuela made similar claims.

Congressional hearings in 1983, on the size and concentration of the exposure of U.S. banks to the developing nations with repayment problems, revealed serious deficiencies in the way banking regulators were supervising international lending. Among other things it was determined that banks were not setting aside sufficient reserves against their loans to foreign borrowers and needed a stronger capital base to ensure their safety and soundness. To remedy deficiencies Congress in 1983 enacted the International Lending Supervision Act of 1983 (ILSA).

Section 905 of ILSA directed the regulators to require that banking institutions establish "special reserves" that did not count as capital against international loans where there was a protracted inability by the public or private borrowers in a foreign country to make payments on their indebtedness. In making this judgement regulators were ordered by ILSA to consider factors such as whether there were failures "to make full interest payments on external indebtedness" or "a failure by the foreign country to comply with an IMF or other suitable adjustment program".

During 1986 the Banking Committee conducted oversight hearings to determine how the regulators were implementing the provisions of ILSA. It was discovered that the provisions of the 1983 Act requiring banks to build "special reserves" against troubled foreign loans were not being implemented in the manner originally envisioned by Congress. The regulators required such reserves to be built against only a very small amount (less than 2 percent) of the more than $116 billion total of the developing country exposure of U.S. banks. The regulators were requiring such reserves only against loans to countries categorized as either "value impaired" or "loss". These are the lowest two categories used by the regulators and loans are only put into these categories when they are worth little or nothing of their book value.

Most loans to the major debtor countries such as Mexico, Brazil, Venezuela and Argentina were placed in the "OTRP" category. This category covers loans to countries, not complying with their external debt-service obligations, but which are taking positive measures, such as an IMF program to regain solvency. The regulators required no special reserves for loans in this category, nor for loans in the next lower category, that is the "substandard" category. This category covers countries that are not servicing their loans nor negotiating with the banks to enable them to do so.

The 1986 hearings revealed that the "special reserves" against troubled loans that Congress required in the 1983 Act were not in place and that U.S. banks were not adequately reserved to take a loss on such loans if that were necessary. The hearings also revealed that a secondary market was developing in most of these troubled loans and that loans classified as "OTRP" or "Substandard" by the regulators traded at varying discounts off their face value. This continues to be the case. A recent article in the American Banker stated that the market is now paying about $0.62 cents for each dollar of Brazilian debt and $0.55 for each dollar of debt to Mexico. The values given these loans by the market fluctuate based on political and economic developments both in the given debtor countries and the world at large. These hearings made it clear, however, that the regulators and banks were not facing up to the realities of their situation with regard to the loans.

These factors led me to sponsor legislation with Senator Gramm (S. 898) to compel our banks to build more adequate reserves against such troubled loans. I also put a provision in the bill I presented for mark up which required banks to build adequate reserves that reflected the market's judgement that losses on these loans were likely. The provision did not require the banks to take any losses, but was designed as a prudential measure in the event the market was right in what it was saying about the value of the developing country debt. Banks in many other countries had already taken such actions.

The big money center banks launched a major lobbying effect to strike this provision of our banking bill on the ground that it would send the wrong signal to the debtor nations. It was argued that the market was not a good indicator of the real value of these loans as it was too thin. It was also argued that the banks have built up their capital from the 1983 period and now the nine money center banks have "only" 140 percent of their capital exposed in Argentina, Brazil and Mexico. It is true that banks have increased their capital since 1982, but so have their total loan portfolios become more troubled. In addition to developing country debt, they now have other troubled loans in their domestic real estate, agriculture and energy market portfolios. Also their off-balance sheet liabilities have increased dramatically. In 1985 alone the off-balance sheet liabilities of the five largest banks increased by twenty-eight percent to more than $1 trillion. That amounted to more than twice their total assets at $545.5 billion and more than 40 times their combined shareholder's equity. The increase in these liabilities is an additional reason why the increased capital of the banks since 1982 did not alleviate concerns about the developing country loans and the need to have adequate reserves against them.

Nevertheless the bank lobbyists were successful in their efforts and the Banking Committee deleted the mandatory reserve provision from title V at the May 19 mark-up. Later that very same day Citicorp announced it was adding $3 billion to its loan loss reserves in an attempt to move the bank out from under the third world loans hanging over its head. The $3 billion amounts to about 25 percent of Citicorp's total loan exposure classified as OTRP or Substandard. In other words that bank did in one quarter what the provision deleted by our Committee, as too draconian and not needed, would have given it up to 5 years to do. Some of the other major banks with Third World exposures have not followed Citicorp's lead. The stock market has even rewarded them for doing so in that with additional reserves the banks are seen to be less vulnerable to the political and economic risks inherent in their developing country loan portfolio.

When asked why Citicorp established its $3 billion loan loss reserve Mr. John Reed, Citicorp Chairman, stated "a bank established loan loss reserves because it thinks it might experience loan losses in the future. * * * Looking at world economic conditions Citicorp's management decided it may not be able to collect all of the $14 billion it has lent to financially troubled third world countries, especially those in Latin America. The $3 billion placed in reserves is only a very rough estimate of the potential loss on that $14 billion * * *"

Although Citicorp and many other banks have now announced they are building loan loss reserves against their troubled international loans because losses may occur on them, their safety and soundness is not really increased. Why? Let me explain.

Bank regulators measure a bank's capital adequacy according to its "primary capital" which consists of equity capital plus loan loss revenues. Before Citicorp increased its loan loss reserve its ratio of primary capital to total assets was about 7 percent. After the loan loss reserve increase, it had the same 7 percent primary capital. All that happened was that its primary capital was shifted from one pocket to another. From a regulatory point of view Citicorp is no stronger.

As noted many banks have now followed Citicorp's lead and are admitting they expect losses on their troubled international loans. While I welcome their new found candor, I do not think the actions they have taken thus far will really increase their safety and soundness.

The Citicorp announcement and Mr. Reed's admission that Citicorp believes $3 billion is a rough estimate of its loss on international loans came after our Committee had already marked up. The Committee might have acted differently on this matter if it had had prior knowledge of Citicorp's decision and the similar actions then undertaken by other banks. It has only strengthened my conviction that the banks must increase their primary capital in order to bolster their safety and soundness.

The full Senate should consider this matter when the Banking Committee's contribution to the omnibus trade bill is taken up on the floor. I will at that time present a proposal that will help ensure this important public policy issue is not just swept under the rug.

WILLIAM PROXMIRE.

ADDITIONAL VIEWS OF SENATOR CRANSTON: TITLE I OF THE TRADE ENHANCEMENT ACT OF 1987

Although the Committee did not address this issue directly, I am concerned about a provision in H.R. 3 which pertains to the exporation of domestically produced crude oil. Section 331 of H.R. 3 changes existing law by prohibiting the export of any domestically produced crude oil to any country except Canada or Mexico. Section 331, rather than plugging a loophole in laws governing Alaska North Slope (ANS) exports, would apply the restrictions on ANS exports to all other domestically produced crude oil.

A blanket prohibition against the export of all domestically produced crude oil is unnecessary and overly restrictive. There is already a myriad of statutes regulating exports of crude oil which protect national security interests. Aside from the Export Administration Act, there are presently four other statutes that restrict export of domestically produced oil from different sources.

The Outer Continental Shelf Lands Act pertains to export of crude oil produced from the Outer Continental Shelf. The Mineral Leasing Act applies to oil transported over federal rights-of-way. The Naval Petroleum Reserves Production Act governs crude oil produced from the naval petroleum reserves. All of these statutes require Presidential findings concerning national security interests and the impact of export on availability or reliance on imported oil sources. The Presidential findings must be submitted to Congress which then may object to export.

Section 103 of the Energy Policy and Conservation Act (EPCA) requires promulgation of a rule prohibiting export of all domestically produced crude oil; however, it authorizes exceptions based on a national interest finding.

I am not convinced that it is necessary or wise, in light of the existing restrictions embodied in current Federal law, to change the law and place a total ban on the exportation of domestically produced crude oil.

ALAN CRANSTON.

ADDITIONAL VIEWS OF SENATORS CRANSTON AND DODD: TITLE I OF THE TRADE ENHANCEMENT ACT OF 1987

We are pleased that the Committee has addressed the important issue of export control reform in the Trade Enhancement Act. However, the Committee bill falls short of the reforms which we believe are necessary to preserve our national security while stimulating our economic growth.

The current export licensing system is choking the genius of this country. The chorus of anecdotes we have heard tells a story of lost sales, withdrawn licenses, and an absence of confidence in our present system of controls. Exporters doubt that licenses will be approved promptly and with a consistent rationale. The recently published National Academy of Sciences report, "balancing the national interest: U.S. national security export controls and global economic competitiveness," states flatly, "U.S. national security controls are not generally perceived as rational, credible, and predictable by many of the nations and commercial interests whose active cooperation is required for an effective system."

Export controls exist to deny the Soviet Union and Eastern bloc countries access to strategic technology that would further those countries' military capabilities. By overcontrolling goods, we believe we are undermining this principle. By refocusing our control resources on higher levels of technology, technology that is truly "critical", we will more efficiently prevent diversion of critical technology to our adversaries while promoting our exports.

Committee Print No. 1 included several worthwhile provisions contained in the High Technology Trade Enhancement Act, S. 652, which was introduced earlier this year: providing distribution licenses to the PRC, decontrolling below the AEN line to free world destinations, eliminating reexport controls within Cocom, and expediting the foreign availability process. We are delighted these were adopted by the Committee.

The package amendment we introduced with several of our colleagues greatly improved the Committee bill and will lead to a more effective and rational export control system. By establishing a West/West foreign availability determination, updating the microprocessor decontrol language in Section 5(M), and working toward the elimination of unilateral controls, we will remove many of the impediments to our exporters' ability to compete. The amendment also attempts to resolve some of the interagency disputes which have bogged down the system. For example, it clarifies Commerce's authority for formulating U.S. positions for Cocom list review and decontrol, provides that Commerce has final authority on foreign availability determinations (ending the de facto veto power of defense), and establishes a mechanism to resolve control list disputes.

We are particularly pleased to see that this bill addresses the role of the Department of Defense. The NAS report states, "the Exclusive DOD focus on tightening export controls without balancing input from other agencies concerning the possible economic and long-term national security consequences has resulted in a failure to bring the objectives of military security and economic vitality into balance." In our opinion, the confusion and incessant in-fighting between agencies is the root problem in our export control system. The Department of Commerce is the lead agency on export controls. Institutional clarification of this fact and of the appropriate role of defense in the process are the most useful reforms we can make.

The Committee bill places strict time limits on the Department of Defense and reiterates that the President is to resolve a dispute within 20 days. The law provides that Commerce can act upon the license if the President fails to make a determination within the stated time period. As in S. 652, the Committee bill also states that the Commander in Chief no longer has to inform Congress when he disagrees with his Secretary of Defense. We believe this astonishing requirement imposed upon the President has been used as a tool of intimidation, has led to undue influence by the Department of Defense, and has caused gridlock throughout the entire export control system.

We commend the chairman and Committee for recognizing the need to make these important changes. Nonetheless, these reforms do not go far enough. While we agree that the Department of Defense has a role to play in the export control process, we should continue to reexamine and better define that role. While the Committee has attempted to address the interagency dispute problem, we believe criticisms of DOD do not stem solely from the lack of timely resolution to such disputes. In my opinion, we must evaluate what unique contribution can be made by DOD. We must also look at the consequences of a "conditional" response by DOD. This occurs when defense returns an application to Commerce recommending approval subject to specified conditions. Commerce, as the lead agency, should consider these conditions as advisory, not mandatory.

The NAS report, written by a blue-ribbon panel of experts led by Lew Allen, former Chief of Staff of the U.S. Air Force, declares, "it should now be the goal (1) to establish greater balance within DOD between its technical and policy elements and (2) to reduce the DOD role in detailed license review as parallel steps are taken within the Department of Commerce to strengthen its capacity to implement national security export control licensing procedures." In addition, last year a GAO study found a high level of consistency on license reviews between Commerce and DOD, and questioned "whether defense review of individual free world license applications should be continued in its present form". The Committee bill fails to address these important issues.

There are other areas where we believe additional reforms would prove beneficial, and there are some sections of the Committee bill which we believe go too far. For example, while we recognize the need for the prior convictions and temporary denial order sections of the law, we think the provisions passed by the Committee are ambiguous and overly broad.

Our export control system would be greatly enhanced by opening a licensing office in the western region. Currently, approximately 120,000 licenses must be processed each year in one Washington, D.C. office. Since 1984, 41 percent of all licenses by value have been from the three west coast States. The disadvantages faced by western exporters are severe and costly. In addition, we believe we could expand general license procedures for temporary exports (GTE) to the Peoples Republic of China. Such action would be consistent with the actions taken by the Committee to improve our economic links with the PRC.

The Kongsberg-Toshiba diversion case has reinforced the need for a strong Cocom. One of the two basic recommendations of the NAS report is to strengthen the Cocom system. The report suggests that further efforts are necessary "to bring about greater harmonization of national policies and to work toward a more rational—and fully multilateral—system of national security export controls." We must recognize that unilateral controls are ineffective and work toward a strong Cocom which can be virtually license-free.

Moreover, it would be both practical and efficient to increase the advisory role of industry representatives: Often it is the industry people who have the best knowledge of state of the art technologies and their applications. The NAS report found that "the U.S. Delegation to Cocom includes a significant contingent from the Department of Defense, but most other Cocom members are represented at Cocom meetings principally by their economic and trade ministries. The panel finds that a balance of economic and defense representation on all the Cocom delegations would enhance Cocom unity and the usefulness of the Cocom process". We support having an industry representative as an advisor at Cocom negotiations and strengthening the role of technical advisory committees.

A great deal of time and energy has been expended in coming up with a committee bill that recognizes the divergent views of the Committee members. While we are generally encouraged by the changes to the Export Administration Act made by the Committee, we feel strongly that additional reforms could be made that would increase our competitiveness without jeopardizing our national security.

ALAN CRANSTON.
CHRISTOPHER DODD.

ADDITIONAL VIEWS OF SENATORS GARN, HEINZ, HECHT, BOND, CHAFEE, AND KARNES

TITLE VII—FOREIGN CORRUPT PRACTICES ACT

The Committee Report underestimates the importance of the "amendments" to the Foreign Corrupt Practices Act of 1977 (FCPA) in Title VII. These are significant changes that will reduce the confusion and ambiguity of the anti-bribery and accounting provisions and substantially remove the FCPA's impact as an export disincentive, while preserving its chief purpose—to outlaw bribery of foreign officials by American corporations. The amendments are needed to improve our position in world export markets, for this will lead to more jobs at home.

The amendments focus on three major areas:

First, the anti-bribery provisions. Currently, companies and related personnel are criminally liable if they know or have reason to know that a bribe, even unauthorized, will be paid to a foreign official, directly or by an intermediary.

The "reason to know" standard, basically a negligence standard, and often after the fact, causes uncertainty and leads to unnecessary caution and a reduced competitive posture. The "reason to know" provision is therefore of great concern to business, and especially problematic for small businesses that often operate through foreign agents. The Justice Department does not favor the "reason to know" standard, calling it "plainly inappropriate" and "harsh and inconsistent with the general approach of modern criminal law to state of mind requirements". The Justice Department has used a knowledge standard in deciding whether to prosecute in both the Carter and Reagan administrations, and has stated it will prosecute cases only where "evidence of awareness is so clear as to constitute actual knowledge of the bribe scheme." The amendments' standard, to "direct or authorize, expressly or by a course of conduct", is therefore clearer and fairer, because it applies to the person who brings about bribery—his behavior will determine culpability. It also generally brings the FCPA's foreign bribery language into conformity with domestic bribery statutes.

The "course of conduct" language also specifically deals with the "head in the sand" approach, where a chairman might "wink" at bribery. The Justice Department has noted that the new standard would "prevent a company or businessman from using an agent or another third party as a protective shield from criminal prosecution"; there is also legislative history on the matter.

In enacting the FCPA, Congress intended not to cover certain payments, made without requisite corrupt intent. The amendments clarify the circumstances under which such payments are allowed, by focusing on the purpose of the payer rather than the status of the payee. This would enable U.S. companies no longer to forego or lose legitimate business opportunities, due to doubts as to what is acceptable. For once export opportunities disappear, they are difficult to recover. However, the amendments retain strong sanctions against making corrupt payments, and the stated permissible payments are all subject to this overarching antibribery thrust of the FCPA.

Second, the accounting standards. Currently, companies are criminally liable for minor or inadvertent errors in the creation and maintenance of accurate records and internal controls that are interrelated components of the general FCPA accounting standards, intended to reveal and protect against corrupt foreign payments. This concern has caused corporations additional expense, often out of proportion to the benefits received. The SEC has stated that such recordkeeping mistakes will not give rise to Commission enforcement proceedings, and supports the view that records be kept "in reasonable detail" using a cost/benefit approach and noncompliance would face civil, not criminal, penalties. It is essential that this view of the agency charged with enforcement be given the force of law. A company is entitled to statutory certainty. However, a person who knowingly circumvents the system or knowingly falsifies books, records, or accounts would be subject to criminal liability.

Third, enforcement. Currently, the division of enforcement can potentially lead to different standards of enforcement being applied to public companies and other persons. The amendments would have the SEC retain responsibility for civil enforcement of the accounting provisions, but the Department of Justice would have all jurisdiction (civil as well as criminal) for enforcement of the antibribery provisions. Thus, any company with questions about the bribery provisions could have them answered in one place.

The amendments have broad support and have been buttressed by the extensive hearing records of the last three Congresses. Predecessor bills, which were similar in the essentials, received strong bipartisan Committee endorsement. The 1981 bill passed the Banking Committee by an 11-4 vote, and the Senate by a voice vote. The 1983 bill passed the Committee by a 17-1 vote, and the 1985 bill by an 11-3 vote. The amendments are endorsed by the Administration, the agencies responsible for enforcement (the SEC and the Department of Justice), and the business community at large (for example, the U.S. Chamber of Commerce, the Emergency Committee for American Trade, and the National Association of Manufacturers).

It is gratifying to see that strong support was again provided in Committee. The Senate should delay no longer in adopting these vital clarifications; neither should the Congress, now that the House has also acted. Our delay in amending the FCPA has increased costs to corporations while causing them to forego or lose legitimate overseas business; this is especially unjustifiable in view of our trade deficit. The law's purpose is clear, but as presently worded, the law is vague and cumbersome. U.S. business must be encouraged to be more competitive, by eliminating longstanding concerns with the FCPA without in any way weakening its prohibition of overseas bribery or diminishing its anti-bribery effectiveness.

JAKE GARN.
JOHN HEINZ.
CHIC HECHT.
CHRISTOPHER S. BOND.
JOHN H. CHAFEE.
DAVID K. KARNES.

ADDITIONAL VIEWS OF SENATOR HEINZ

The bill reported by the Banking Committee contains many important and worthwhile provisions that will improve prospects for U.S. trade in the years ahead. The strongest portions of our bill are those developed through the kind of bipartisan debate that has long characterized the Committee's approach to international issues or those based on past Committee consensus. Notable in this regard are the titles on export controls and the Foreign Corrupt Practices Act. While there are no doubt ways in which both titles could be improved, they enjoy the support of a substantial majority of the Committee.

Other titles of the bill are notably weaker for the lack of consensus they represent. The debt issue, for example, was a topic of considerable dispute at mark-up and the only agreement the Committee could reach on dealing with the problem was a series of reports and studies. The only operative provision in the Committee Print attempted to enforce substantial bank reserves against troubled LDC loans. It was billed as a "bank safety" provision but would have all but eliminated already weak cooperation between banks and debtors and worsened the bank safety problem as a result. No effort was made to craft a proposal supported by more than a small minority of the Committee and it was overwhelmingly rejected as a result. The Committee bill is therefore silent on a point it has previously regarded as very significant.

The debt title does include language calling for a broader range of options in addition to new lending for dealing with the debt problem. It calls for the start of discussions regarding creation of a debt management facility to buy debt as a discount from banks and pass along the discount to LDC debtors. It also recognizes that creditors must explore a broader range of financial options for creditor support including debt-equity conversions and some forms of debt relief, and commissions various studies of these mechanisms and impediments to their use. The greatest flaw in these provisions is that, in the face of immediate financial difficulties, they offer only discussion and analysis to the debtor countries. A debt facility would take years to formulate and negotiate, even if it did not face the duel burden of opposition from the Administration charged with negotiating it, and likely congressional opposition if its eventual price tag is large.

One substantive option that the Committee considered was a change in the Bank Holding Company Act to expand the range of investments for which banks could swap their troubled LDC loans. This would have made a modest contribution to expanding LDC investment and reducing their debt service. However, the Committee opted to stick with regulatory studies in the Committee Print that ask the regulators to report back next year on what is wrong with the way they now regulate debt-equity swaps and other debt management techniques. By the time they tell the Committee that they are doing everything right, the Europeans and Japanese will have already swapped for every sound equity investment in Latin America.

EXPORT TRADING COMPANIES

The other title of the bill with greatest problems is Title II, the Export Trading Company Act amendments. Last year, the Committee reached near unanimous agreement on solutions to the problems facing ETCs regarding allowable ETC activities in facilitating third-country trade and direct provision of services, leverage and inventory. Our Committee Print failed to build upon this past consensus, instead adopting seriously flawed language developed by the House Banking Committee. The Print tracks past Committee language only on inventory. It takes half-way measures on leverage and third-country trade, and is silent on trade in services. At mark-up, an attempt to substitute past consensus solutions failed on a tie vote.

The failure to reach a consensus this year is difficult to understand given the history of this issue in the Committee. The Banking Committee began the legislative process to promote formation of U.S. export trading companies in 1979. When the ETC Act became law in 1982, it represented an important evolution of our bank regulatory laws that permitted banks to link their expertise in financing with a range of trade-related, nonbanking activities. As time passed, however, it became clear that the law was not working as intended.

Last year, the Committee held hearings that demonstrated the crippling impact of overly cautious Federal Reserve regulation on our ETC's ability to compete. We learned that the Fed discourages ETCs from earning income and developing business contacts through facilitation of third-country trade. The regulations prevent ETCs from offering the full range of trade services authorized in the 1982 law. They also deny ETC applications a fair hearing because of narrow limitations on ETC leverage and inventory. Last September, the Committee reported a series of amendments to rationalize these Fed regulations. The amendments were reported by voice vote, and objection was raised to only one provision and that by a single Member.

Since these amendments were not enacted last year, the Committee returned to the problems of our U.S. trading companies in March hearings. The Committee heard the same lament from our bank ETCs and the same saga of excessive controls from the Federal Reserve. We faced the same challenge to correct problems in the key areas of third-country trade, trade in services and ETC leverage.

Rather than fixing the problems identified by the Committee once and for all, however, this bill takes halting steps that simply do not solve the problems.

On third-country trade, the right to facilitate such deals is at least recognized in the Committee bill. But instead of fixing the problem cleanly, the bill adds requirements that fees count only if remitted to the United States and only to the extent the aggregate amount is less than 20 percent of export revenues.

The remittance requirement is intended to ensure that third-country fees add to U.S. service income. Instead it unnecessarily complicates ETC accounting with marginal effect on the U.S. trade balance. Almost all ETC business is currently done and all fees earned by ETC offices in the United States; remitting income is irrelevant. Where deals are arranged through overseas offices of an ETC's parent bank, the fees earned are already counted as U.S. service income under national income accounting rules. Only if an ETC opens and does business through an overseas affiliate would the remittance requirement have the effect of ensuring fees earned counted as service income. But even if such cases arise, it would seem to matter little to the U.S. payments position if the ETC used a fee earned abroad for working capital and remitted net income earned at the end of the year rather than remitting every fee earned to meet the Federal Reserve's revenue test.

The limitation on the amount of third-country trade is also counterproductive. It is based on the notion that if left to their own devices, ETCs would forget their U.S. customers, deal only in third-country trade, and somehow harm the U.S. trade position. These conclusions are difficult to accept.

Banks set up ETCs primarily to assist their domestic customers to export. It is unlikely that a U.S. bank would permit its ETC to ignore these customers or that an ETC would ignore this customer base in favor of devoting all its resources to finding new customers in third countries. In those cases where new customer relationships were established through third-country deals, this would likely create new business opportunities for American exporters not replace them. In addition, the fees ETCs earn on these deals add to U.S. export income directly.

This is not a theoretical proposition. In one recent case, a bank ETC turned down an opportunity to handle trade between South Korea and China because the third-country earnings would have endangered their ETC qualification. A major income opportunity was lost, along with the chance to develop trade contacts in key Asian markets. The transaction would even have aided U.S. foreign policy objectives.

Japanese ETCs, the model for aggressive trading, earn fees on third-country trade equal to more than 40 percent of export income. I know of no one who thinks these $300 plus billion trading companies are damaging Japan's trade position as a result. Expanded world trade in which U.S. firms are involved and on which they earn service income is clearly beneficial to the United States. We should not be tying the hands of our ETCs and discouraging trade in the process.

The Committee bill ignores the vital issue of ETC trade in services. The ETC Act sets out a non-exclusive list of services in which ETCs are permitted to engage, ranging from advertising to warehousing. Despite the fact that provision of these services expands U.S. export income without threatening bank safety and soundness, the Federal Reserve Board has effectively vetoed this provision of law. It is essential that its narrow interpretation of the law which effectively precludes ETCs from direct provision of most services be corrected, yet the Committee bill is silent on the matter.

Finally, on the issue of ETC leverage, the Committee bill again acknowledges that current Fed regulation is excessively tight but stops short of solving the problem. The Federal Reserve now discourages ETC applications if they call for a debt-to-capital ratio greater than 10:1. This is considerably tighter than the 17:1 leverage requirement for a parent bank, yet for an ETC to operate successfully as a direct exporter, it must undertake substantial borrowing to fund a large volume of trade transactions. By comparison, Japanese ETCs operate with ratios as high as 50:1.

This Fed requirement is a major hurdle for young ETCs as they try to build up a volume of trade deals on a necessarily modest capital base. The Committee bill raises the permissible leverage level but only to 15:1, still below the parent bank's level. It leaves the Fed with authority to turn down an ETC application based only on a proposed leverage level even where the ETC's proposed leverage is more conservative than that of its parent bank.

I believe that the Committee has consistently focused on the key problems facing our ETCs, but has reported legislation that simply fails to correct them. I do not believe that this is what the Committee intended and hope that when Members review the outcome, they will share my view that those solutions it strongly endorsed in the past are the right ones. Only then can we encourage the growth of aggressive export trading companies that must be part of the U.S. exporting infrastructures.

JOHN HEINZ.

ADDITIONAL VIEWS OF WILLIAM L. ARMSTRONG

It is human nature to observe the failings of someone else while ignoring the very same flaws in oneself. This trait is apparent in this legislation reported by the Senate Banking Committee.

With crushing debt burdens at home and abroad, it is interesting to witness the degree to which the majority of this committee devotes itself to alleviating the debt burden of third world countries on the pretext of improving U.S. trade imbalances, while ignoring the very same problems at home. In the very same year the committee lectures about the need to reduce third world debt, the committee has taken the lead in passing budget busting legislation that actually contributes to our trade imbalance.

Convincing testimony was presented that the Congress could be more effective in rectifying trade imbalances by addressing our domestic federal budget deficit. That advice went unheeded as it might have called into question the fact that the very same committee reported mass transit and housing legislation that together was $12 billion over the President's recommendations.

So it is with some skepticism that I view substantial portions of this "Export Enhancement Act of 1987." The legislation reported by this committee includes seven major titles that range from promoting U.S. trade to revamping the international monetary order.

The first three titles respond to the imperative of reducing bureaucratic delay and restraints on export sales of U.S. products. Goods, services and technologies that are defense-sensitive also benefit from the changes in trade procedures where there is no compromise to national security. If any or all of these changes can alleviate the frustrations of having the know-how, having the capability and having the product—but not having the ability to make the international sale, then Bravo! I'm all for it.

I become somewhat more cautious when the committee ventures into the area of initiating multilateral negotiations to "institutionalize the process of coordinating monetary and fiscal policies * * *" as it does in Title IV without a better idea of where we are going and why. Is this to be the international monetary policy equivalent of the United Nations?

With the advent of economics, trade and financial markets moving to a global scale, much needs to be comprehended and analyzed. Past efforts at coordinating exchange rates and monetary and fiscal policies have met with very mixed results. The ambiguous ideas presented by this part of the legislation to institutionalize the enigmas of world monetary policy interactions into an international organization of unknown influence seems to be a course of action that is exceedingly imprecise. There are very significant foreign policy considerations to such an action and any move in this direction should have considerable influence from the executive branch of government and be quite quite explicit.

Yet if all Title IV comes down to is just an annual report by the Secretary of Treasury to Capitol Hill that discusses exchange rates, I would hate to claim victory over trade imbalances on that provision alone.

ON LDC DEBT FACILITY

What I find most troublesome in this trade package is Title V. It establishes a structure to forgive portions of LDC debt held by U.S. banks. I have never been one to sympathize with our capital being taken from use at home and lent overseas. Once done, I see few reasons to forgive portions of it either. We have lost the use of the capital and this proposal would have us reduce the income flow from it as well. This happens at the very time when investment in this country is extraordinarily dependent on foreign sources, a fact that is exacerbated by declining U.S. interest rates.

The relationship between debtor countries and their creditors has always demonstrated a resourcefulness that has been assisted at times by the Treasury Department and multilateral banks. These existing mechanisms have operated to mutually assist each other and I believe they can continue to manage the risks they have assumed contrary to a "finding" of the legislation that "existing mechanisms for resolving the debt crisis have failed to produce adequate new capital flows * * *".

The "findings" set out in this title that comprise the premise for such a write-down proposal are subject to challenge. Title V sets out eleven findings on which the proposal is based. Many of these findings can and have been challenged by many including Federal Reserve Board Chairman Paul Volcker.

Finding #1 states the "international debt crisis threatens the safety and soundness of the international financial system * * *" Chairman Volcker stated before the committee on April 7th that debtor countries have done much to improve their internal discipline saying "I think more progress has been made in this direction in the past few years than has been made in the previous 50 years * * *"

Finding #3 states the obvious that "growth in developing countries with substantial external debts has been severely constrained * * *" Volcker notes "* * * that the level of world interest rates has declined and, and as a consequence, the burden of external interest payments has been falling, despite some increases in debt."

Finding #5 states that "negative resource transfers at present levels severely depress both investment and growth in debtor countries * * *" Volcker called the argument that capital provided to LDC countries in being diverted away from new activities to pay old debt as being a "red herring" since money is fungible and "Any borrower that is in the market is in effect borrowing to pay interest the old debt."

Despite the misguided "findings" this proposal suffers from more basic conceptual flaws. If a writedown of LDC loans permits some forgiveness of a country's debt that translates into economic gains for those countries and improved markets for U.S. exports, jobs and prosperity, I am yet to be convinced. With more money to spend what will these LDC's buy from America? Automobiles, dishwashers, steel, computers? The more likely result will be that citizens of LDC's will buy what they need most, the basic necessities which are typically domestic or regional expenditures.

To the degree they are able to purchase more from abroad, they will be equally able to purchase items from Japan, western Europe as from the United States. The connection between LDC loan write-downs and U.S. jobs and exports is tenuous indeed.

If this country wishes to devote less of its political and economic resources toward making abstract proposals to improve the debt problems of foreign nations and devote the same resources to the same fiscal issues that face this country, there is an answer.

The answer was presented in no uncertain terms to the Senate banking committee on April 7th, again by Paul Volcker, when this question was asked of him by Senator Gramm:

> GRAMM. If Congress has the objective of lowering the trade deficit, bringing down interest rates, creating jobs and stimulating increases in prosperity and real wages in this country, what would you think would be the most efficient and effective one thing that we could do to promote all those goals?
>
> VOLCKER. Reduce the budget deficit.
>
> GRAMM. Say it again.
>
> VOLCKER. Reduce the budget deficit.
>
> GRAMM. Got it.

Chairman Volcker explained his reasoning later:

> If you don't deal with the budget deficit, you are forcing us to rely upon foreign savings and that is another fancy way of saying you're forcing a trade deficit because the only way you can draw on foreign savings is by running a trade deficit.

Title IV and V of the "United States Trade Enhancement Act of 1987," move away from problem solving and into uncharted waters. These two questionable titles embody the continuing dilemma for the majority and that is the tendency to establish bureaucracies without solutions and to use our political capital to eradicate problems overseas when the very same problems at home go unattended.

I wonder why the Congress doesn't devote more attention to the debt problems in the United States; since 1985 a net debtor nation. The answer that would help everyone, worldwide, is obvious: Reduce the federal budget deficit. A good place to start would be in the Banking Committee.

WILLIAM L. ARMSTRONG.

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